CAIIB MADE SIMPLE

ADVANCED BANK MANAGEMENT

(CAIIB PAPER -1)

Version 1.0

(A Very useful book for Day to Day Banking and all Knowledge Based Examinations)

COMPILED BY

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Preface

Dear Friends,

Banking/Financial sector in our country is witnessing a sea change & banker's business has become more complex & difficult in this driven era of knowledge & technology. There are mass retirements happening due to super annuation & many new recruits are joining the Bank. More than 40% staff strength is newly recruited in last three to four years. An official working in the Banking sector has to keep pace with Updated knowledge, skills & attitude, as the same is required everywhere. There is need to issue a comprehensive book covering all the aspects so that new recruits get updated very fast without referring many voluminous books.

This book titled " CAIIB MADE SIMPLE " has many unique features to its credit & consists of all topics/syllabus required for CAIIB examination with clear concept & simple language with latest changes during 2015-16 (upto June/July 2015 as per IIBF/ CAIIB exams.requirement) also included. This Book is divided into four Modules namely A, B, C & D with Practice Teat Papers / Teat Yourself based on latest IIBF syllabus for CAIIB examination.

The Book also covers the full syllabus (latest) of CAIIB examination and also recalled questions & MCQ based on IIBF examination Pattern will be helpful to all aspirants who are taking up CAIIB examination

During preparation of this book, I have received tremendous support from Team RSTC, Mumbai, many friends & colleagues especially Sri V Manoj from RSTC, Guwahati, my wife Mrs Renu, who is also a banker, my son Master Ritwiz Aryan & Special thanks to Sri B P Desai Sir (Our Ex. AGM & now Faculty on Contract at RSTC, Mumbai) for vetting & compilation of this book.

As any work will have always scope for further improvement, I shall be grateful if any feedback is provided for improvement in contents of the book.

I wish you all the best for the written test & hope the study material will help in achieving the goal.

Place : Mumbai
Date : 02.12.2015

SANJAY KUMAR TRIVEDY
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ABOUT CAIIB EXAMINATION

CAIIB EXAMINATION – Dec 2015

OBJECTIVE:

CAIIB aims at providing advanced knowledge necessary for better decision making covering risk, financial and general bank management.

MEDIUM OF EXAMINATION : Either in Hindi or English
ELIGIBILITY : Candidates must have completed JAIIB or PART-1 of the Associate Examination, and their membership subscription should not be in arrears.
SUBJECT OF EXAMINATION
I. Compulsory Paper

1. Advanced Bank Management
2. Bank Financial Management

II. Elective Papers (Candidates to choose any one of their Choice)

1.	Corporate Banking	7.	Human Resources Management
2.	Rural Banking	8.	Information Technology
3.	International Banking	9.	Risk Management
4.	Retail Banking	10.	Central Banking
5.	Co-operative Banking	11.	Treasury Management
6.	Financial advising		

There is no exemption in any of the above subject/s for prior qualification/s.
The Institute has introduced electives to give opportunities for candidates to specialize in the vertical of their choice. Candidates may choose the elective in the area they are currently working or in the area they would like to work in future. It is suggested that the candidates may choose the elective in the area they are currently working and later move to other elective as this will enable appropriate skills / build up for handling different banking verticals.

Cut-off Date of Guidelines / Important Developments for Examinations
In respect of the exams to be conducted by the Institute during May / June of a calendar year, instructions / guidelines issued by the regulator(s) and important developments in banking and finance up to 31st December of the previous year will only be considered for the purpose of inclusion in the question papers. In respect of the exams to be conducted by the Institute during November / December of a calendar year, instructions / guidelines issued by the regulator(s) and important developments in banking and finance up to 30 June of that year will only be the considered for the purpose of inclusion in the question papers**. (This has been taken from IIBF – Vision Monthly Magazine , June 2015, Page no. 7)**
Further, questions based on current developments in banking and finance may be asked. Candidates are advised to refer to financial news papers / periodicals more particularly "IIBF VISION" and "BANK QUEST" published by the Institute.
MODE OF EXAMINATION
Examination will be conducted in Online Mode at majority of centres and under offline mode (paper and pencil) at selected centres as per the notification given on the web site in this regard. Examination will be held on three consecutive Sundays (one paper on each Sunday).

PROCEDURE FOR APPLYING FOR EXAMINATION
Application for examination should be made online from the Institute's website **www.iibf.org.in**. No physical form

will be accepted by the Institute with effect from 1 January, 2013.

PATTERN OF EXAMINATION : Each Question Paper will contain approximately 100 objective type multiple choice questions, carrying 100 marks including questions based on case study / case lets. The Institute may, however, vary the number of questions to be asked for a subject. There will NOT be **negative marking** for wrong answers.

Further, questions based on current developments in banking and finance may be asked. Candidates are advised to refer to financial news papers / periodicals more particularly "IIBF VISION" and "BANK QUEST" published by the Institute.

Questions for the CAIIB Examination will be asked for :

(a)Knowledge testing, (b) Conceptual grasp, (c) Analytical / logical exposition, (d) Problem solving, (e) Case analysis

TYPES OF QUESTIONS

120 Objective Type Multiple Choice Questions - carrying 100 marks – 120 minutes and question will be based on Knowledge Testing, Conceptual Grasp, Analytical / Logical Exposition, Problem Solving & Case Analysis

A. MULTIPLE CHOICE (Each Questions 0.5 Marks)– QUESTIONS & ANSWERS (60-70 QUES)

B. MULTIPLE CHOICE – (Each Questions 01 Marks)– PROBLEMS & SOLUTIONS (10-15 QUES)

C. MULTIPLE CHOICE – (Each Questions 02 Marks)– APPLIED THEORY – QUES. & ANS. (10 -14 QUES)

D. MULTIPLE CHOICE – (Each Questions 02 Marks)– CASE STUDIES & CASE LETS (PROBLEMS & SOLUTIONS) (12-15QUES)

<u>QUESTIONS MODELS : TYPES OF QUESTIONS</u>

Type – A : MULTIPLE CHOICE – QUESTIONS & ANSWERS

The Best Method for assessing working capital limit used by the bank for seasonal Industries is :
1. Operating Cycle Method, 2. Projected Networking Method, 3. Projected Turn over Method & 4. Cash Budget Method

Type – B : MULTIPLE CHOICE – PROBLEMS & SOLUTIONS

Mr. Ram Kumar is having overdraft account with Canara bank upto Rs.100,000. The present Debit Balance in the account was Rs. 80550.00. The bank has received attachment order from Income tax deptt. For Rs. 16,200.00. What can the bank do in this situation ?

- Unless the bank is a debtor, there can be no attachment and an unutilized overdraft account does not render the bank a debtor (but creditor) & hence can not attach.

Type – C : MULTIPLE CHOICE – APPLIED THEORY – QUES. & ANS

Financial Institution wish to have the money lent by them repaid in time. Secured advances sanctioned by banks possess what kind of security ?

- Secured Advances have impersonal security i.e. Tangible Security

Type –D : MULTIPLE CHOICE – CASE STUDIES & CASE LETS (PROBLEMS & SOLUTIONS)

Economic development of a country to a large extent depends upon Agril. & Industrial sectors. Development of agril. Depends upon irrigation facilities while industrial development on availability of power, good transport and fast communication facilities. All these are called infrastructure. Read the case let & explain which

industries constitute infrastructure ?
a. Energy, Transport & Communication
b. Irrigation, construction of bridges & dams over Rivers & stable govt. at Centre.
c. Availability of Funds for PMEGP , SJSRY & Indira Awas Yojana

DURATION OF EXAMINATION: The duration of the examination will be of 2 hours.

PERIODICITY AND EXAMINATION CENTRES

The examination will be conducted normally twice a year in May / June and November / December on Sundays.

Pass: Minimum marks for pass in every subject - 50 out of 100 marks.

Candidate securing at least 45 marks in each subject with an aggregate of 50% marks in all subjects of CAIIB examination in a single attempt will also be declared as having passed JAIIB Examination.

Candidates will be allowed to retain credits for the subject/s they have passed in one attempt till the expiry of the time limit for passing the examination as mentioned bellow,

TIME LIMIT FOR PASSING THE EXAMINATION

Candidates will be required to pass CAIIB examination within a time limit of 2 years (i.e. 4 consecutive attempts). Initially a candidate will have to pay examination fee for a block of one year i.e. for two attempts. In case a candidate is not able to pass CAIIB examination within 1st block of 2 attempts, he / she can appear for a further period of 1 year (2nd block) i.e. 2 attempts on payment of requisite fee. Candidates who have exhausted the first block of 2 attempts, should necessarily submit the examination application form for the next attempt, without any gap. If they do not submit the examination form immediately after exhausting the first block, the examination conducted will be counted as attempts of the second block for the purpose of time limit for passing.

Candidates not able to pass CAIIB examination within the stipulated time period of two years are required to re-enroll themselves afresh by submitting fresh Examination Application Form. Such candidates will not be granted credit/s for subject/s passed, if any, earlier.

Attempts will be counted from the date of application irrespective of whether a candidate appears at any examination or otherwise.

"CLASS OF PASS" CRITERIA

The Institute will consider the FIRST PHYSICAL ATTEMPT of the candidate at the examination as first attempt for awarding class. In other words, the candidate should not have attempted any of the subject/s pertaining to the concerned examination any time in the past and has to pass all the subjects as per the passing criteria and secure prescribed marks for awarding class. Candidate re-enrolling for the examination after exhausting all permissible attempts as per the time limit rule will not be considered for awarding class.

First Class: 60% or more marks in aggregate and pass in all the subjects in the FIRST PHYSICAL ATTEMPT.
First Class with Distinction: 70% or more marks in aggregate and 60 or more marks in each subject in the FIRST PHYSICAL ATTEMPT.

CAIIB EXAMINATION –Dec 2015
(Last date for applying for examination : 10/09/2015)

ONLINE MODE		
Examination DATE	TIME	SUBJECTS
06/12/2015 Sunday	ONLINE - Will be given in the admit Letter	Advanced Bank Management
13/12/2015 Sunday	ONLINE - Will be given in the admit Letter	Bank Financial Management
20/12/2015 Sunday	ONLINE - Will be given in the admit Letter	Corporate Banking Rural Banking

		International Banking Retail Banking Co-operative Banking Financial Advising Human Resources Management Information Technology Risk Management Central Banking Treasury Management
Last Date for receipt of Change of Centre Requests at the respective Zonal Offices for the CAIIB/Electives Examinations scheduled for Dec 2015 : 30th October 2015		

Revised Examination Fees inclusive SERVICE TAX @14% with effect from 1st June, 2015

(Examination Eligible for Members Only)			
Sr. No.	Name of the Exam	Attempts	For Members(Rs)
1	CAIIB	First Block of 2 attempts	3078
		Second Block of 2 attempts	3078

Module: A

Economic Analysis

SYLLABUS

The fundamentals of Economics: Scarcity and Efficiency - Microeconomics & Macroeconomics in brief - Types of economies - Market, Command and Mixed Economies - Macroeconomics: Business cycles - Money and banking - Unemployment & inflation - Interest rate determination and various types of interest rates.

Indian Economy (a) Overview of the Indian economy including recent reforms (b)Interaction between fiscal, monetary & exchange rate policies in India - Financial Markets (i) Money Market (ii) Capital Market (iii) Foreign Exchange Market - globalisation and its impact - Challenges ahead - Banking & Finance - current issues

THE FUNDAMENTAL OF ECONOMICS

Economics is a social science. It is one of the most important branches of knowledge at present. In this branch of knowledge we try to understand how the economy of a particular region, a country or the global economy works. The term 'Economics' owes its origin to the Greek Word 'Oikonomia' meaning household. The ancient Greeks applied this to the management of a city state, which they called 'Polis'. Thus political economy came into existence. It emerged as a full- fledged social science in the latter half of the 18th Century with the publication of Adam Smith's master piece,

Economists have given different definitions of Economics from time to time as per their understanding of different situations needing attention for economic solutions. Few of the definitions given by renowned economist are discussed below for understanding of the subject matter.

A) <u>WEALTH DEFINITIONS:</u>

This definition of economics is propagated by Adam Smith, David Ricardo, J.B.Say and J.S.Mill. They have assumed Economics as a science of wealth.

"Economic is a subject concerned with an enquiry into the nature and causes of wealth of **nations"- Adam Smith**

"Economic is a science which treats of wealth" - **J.B. Say.**

"Economics is the name of that part of knowledge which relates to wealth" — **Walker.**

The Science which treats of nature, production and distribution of wealth is economics" — **Daven Port.**

"Economics is a science of wealth in relation to man" — **J.S. Mill.**

B) <u>WELFARE DEFINITIONS:</u>

Alfred Marshall was the first economist who **shifted emphasis of economics from wealth to welfare.** Other economists who joined this thought of stream are Prof. Cannon, Prof. A.C. Pigou and Prof. Penson.

"Political economy or economics is a study of mankind in the ordinarily business of life, it examine that part of individual and social actions which most closely connected with the attainment and with the use of material requisites of well being" — **Alfred Marshall.**

"**Aim** of political economy is the explanation of general causes on which the material welfare of the human beings depends" — **Prof. Cannon.**

"Economics is the study of Economics welfare, economic welfare being that part of social welfare which can be brought directly or indirectly into relation with the measuring rod of money" — **Prof. A.C. Pigou.**

"Economics is a science of material welfare" — **Prof. Penson.**

The important features of Marshall's definition are as follows:

Economics studies only the ordinary business of life. Ordinary business of life relates to what a normal human being ordinarily does for his living. In other words, it includes the income earning and income-spending activities of the human beings.

Economics is a social science. It studies the economic problems of those individuals who live in an organized society. Men like Robinson Crusoe living aloof from the society do not fall under the purview of economics.

Economics studies only the material requisites of well-being. There may be other, viz, political, social, and religious activities of human beings. But these activities cannot be measured through the measuring rod of money. Therefore, Marshall restricted the scope of economics to the study of only those economic activities which can have a money measure.

C) <u>SCARCITY DEFINITIONS:</u>

Prof. Robin developed this definition of economics, According to Robin, "Economics is a science which studies human behaviour as a relationship between ends and scarce means, which have alternative uses".

The definition of Robbins brings home the following fundamental conditions:

Economics is a science a positive science. As a science it studies how the human beings adjust their multiple wants to scarce mean. Economics is, therefore, not related to the welfare 6-6 such. Economics studies human behaviour. It is the choice-making behaviour not related to welfare as such, but to ends and scarce means. Ends: Ends. refer to the human wants which are unlimited. Man has multiple wants. As one particular want is satisfied, another want emerges. Therefore, all wants can never be satisfied in their totality.

<u>Scarce Means</u>: Human wants are unlimited, while the means (material resources, time, etc.) to satisfy them

are scarce. Man is confronted with the economic problem when the supply of resourses is short as compared to their demand. Most of goods satisfying human want have limited supply. When resources are scarce, certain wants go **unsatisfied.**

Alternative uses of scarce means: There would have been no problem of allocation, had the scarce means only single use. But, the real difficulty arises because the means have alternative uses and all uses do not have the same intensity. Choice is to be made between the different uses. When we opt for one thing we have to forgo the other.

ID) WANTLESSNESS DEFINITIONS:

This definition is given by **Prof. J.K. Mehta.** According to the definition, "Economics is a Science that studies human behavior as a means to the end of wantlessness". Wantlessness means a process of reducing number of wants to "zero - wants" level. According to **Prof. Mehta** our ultimate goal should be to reach at a stage of wantlessness.

E) GROWTH-ORIENTED DEFINITIONS:

Growth oriented definitions are based on the concept of economic development. Some of the important growth oriented definitions are given below:

"Economics is a study of how, in a civilized society" one obtains a share in what other people have produced and of how the total product of society changes and is determined" - **Henry Smith.**

"Economics studies human behaviour which is concerned with changes and growth in means in relation to growth" **K.G. Seth**

"Economics is a study of the factors affecting employment and standard of living" - **Benham**

"Economic is the study of how men and society choose with or without the use of money to employee scarce productive resources which could have alternative uses to produce various commodities over time, and distribute them for consumption now and in future among various people and groups of society" - **P.A. Samuelson.**

"Economics is a study of the Economic allocation of scares physical and human being among competing and, an allocation that achieves a stipulated opiiiiiizing or maximising objectives". - C.E. **Feruguson**

Economic as a Positive Science

According to Classical, the science of economics should be concerned only with "what is" and not "what ought to be". In other words they maintained, economics is only a positive science. According to Classical school of thought, "Economics should not explain rightness and wrongness of things and economists should not pass moral judgements".

Economics as a Normative Science

Marshall, Pigou and Historical School, challenged the classical school, according to them economic is a normative science because it has norms, viz., more practical, more realistic, useful science, maximum welfare from limited resources and growth oriented.

Micro and Macro Economics

Microeconomics

1. Micro economics is a branch of economics that studies how households and firms make decisions to allocate limited resources, typically in markets where goods or services are being bought and sold.
2. Microeconomics examines how these decisions and behaviours affect and supply and demand for goods and services, which determines prices; and how prices, in turn, determine the supply and demand for goods and services.
3. Microeconbmics analyses the market behavior of individual consumers and firms in an attempt to understand the decision-making process of firms and households.

Macroeconomics:

1. Macro economics is concerned with the overall performance of the economy.
2. Macroeconomics did not exist in its modern form until 1936, when John Maynard Kaynes published his revolutionary book titled *General Theory of Employment,* Interest and Money.
3. In his new theory, Keynes developed an analysis of what causes business cycles, with alternating spells of high unemployment and high inflation.
4. Macroeconomics examines a wide variety of areas, such as how total investment and consumption are determined, how central banks manage money and interest rates, what cause international financial crises, and why some nations grow rapidly while others stagnate.
5. **Macroeconomics** is a branch of Economics that deals with the performance, structure and behavior of

a national or regional economy as a whole.

6. It is the study of the behavior and decision-making of entire economies.

7. Macroeconomists study aggregated indicators such as GDP, unemployment rates and price indices to understand how the whole economy functions.

8. Macroeconomists develop models that explain the relationship among such factors as national income, output, consumption, unemployment, inflation, saving, investment, international trade and international finance.

9. Microeconomics is primarily focused on the actions of individual agents, such as firms and consumers, and how their behavior determines prices and quantities in specific markets.

TYPES OF ECONOMIES

Three fundamental problems faced by any economy: what commodities are produced, how these goods are made, and for whom they are produced.

1. A society must determine how much of each of the many possible goods and services it will make and when they will be produced.

2. How are goods produced?: A society must determine who will do the production, with what resources, and what production techniques they will use.

3. For whom are goods produced? Who gets to eat the fruit of economic activity? Is the distribution of income and wealth fair and equitable? How is the national product divided among different households? Are many people poor and a few rich? Do high incomes go to teachers or athletes or auto workers or venture capitalists? Will society provide minimal consumption to the poor or must people work if they are to eat?

MARKET, COMMAND, AND MIXED ECONOMIES: There are basically two ways of organizing an economy. In the first method, government makes most economic decisions, with people on top of the hierarchy giving economic commands to those further down the ladder. In the second method, decisions are made *in* markets, where individuals or enterprises voluntarily agree to exchange goods and services, usually through payments of money.

Market Economy/Capitalistic Economy:

1. in major parts of the world, and in the United States, there is concept of market economy.

2. A market economy is one in which individuals and private firms make the major decisions about production and consumption.

3. A system or prices, of markets, of profits and losses, of incentives and rewards determines what, how, and for whom.

4. Firms produce the commodities that yield the highest profits (the what) by the techniques of production that are least costly (the how).

5. Consumption is determined by individuals' decisions about how to spend the wages and property incomes, generated by their labour and property ownership (for whom).

6. The extreme case of a market economy, in which the government does not interface in economic decisions, is called a laissez-faire' economy.

Socialistic Economy/Command Economy:

1. A command economy is one in which the government makes all important decisions about production and distribution.

2. In a command economy, the government owns most of the means of production (land and capital); it also owns and directs the operations of enterprises in most industries; it is the employer of most workers and tells them how to do their jobs; and it decides how the output of the society is to be divided among different goods and services.

3. In short, in a command economy, the government addresses major economic questions by virtue of its ownership of resources and its power to enforce decisions.

Mixed Economy:

1. No contemporary society or economy falls completely into either of these extreme categories. Rather, all societies are mixed economies, with elements of both market and command economies. There has never been a 100 per cent market economy.

2. Today most decisions in the United States are made in the marketplace. But the government plays an

important role in overseeing the functioning of the market; government passes laws that regulate economic life, produce goods and services, and control pollution. Most societies/nations today operate as mixed economies.

3. India, right from the beginning of its economic planning, has been a mixed economy where public sector, private sector and joint coexist and complement each other.

Supply and Demand

Demand

Demand is the desire backed by ability and willingness to pay for a commodity

Demand generally means the desire or want for a thing. But in Economics mere desire or want for a thing is not demand. Only when the desire for a commodity is backed by the ability and willingness to pay for it, the desire becomes demand. A commodity may be any good that is produced for sale in the market. In

economics, market means all the areas in which buyers and sellers are in contact with each other for the purchase and sale of a commodity. Demand for a commodity is always at a price. A person's demand for a commodity varies according to its price. At a lower price he will buy more of a commodity and only less at a higher price. The basic unit of consumption is the individual household. It is, therefore necessary to know the individual households' demand for a commodity.

LAW OF DEMAND

Law of demand states the relationship between price and demand of a commodity. As per the law, on change in *price* of a commodity, its *demand* also changes. For instance, decline in price may lead to increase in demand (but other things being equal) or increase in price may lead to decline in demand. This relationship is generally inverse (i.e. moves in opposite direction) relationship.

DEMAND SCHEDULE

Demand schedule provides the information regarding different quantities of a commodity demanded, by a consumer or all consumers at different prices. Demand schedule can be drawn for an individual or for the whole market.

The demand curve, both for the individual or for the whole market, generally shows downward slope from left to right.

Expansion I Contraction of Demand and
increase I decrease in demand

Whenever there is any change in the quantity demanded of a commodity as a result of change in *price,* it is called expansion or contraction of demand. But whenever there is change in demand due to *factors other than price,* it is called increase / decrease in demand.

Similarly, the difference between change in quantity demanded (i.e. expansion or contraction in demand) and change in demand (i.e. increase or decrease in demand) arises because of price and non-price factors respectively as explained above.

Expansion or contraction (or change in quantity demanded)	Due to change in price of a commodity
Increase or decrease in demand (or change in demand)	Due to factors other than change in price

Shifting of demand curve

When whole demand curve shifts either forward or backward, it is called shifting of demand curve.

DIFFERENT KINDS OF DEMAND

Price demand (change in demand due to change in price)

The price demand is the demand of a particular commodity at a particular price. As per the Law of Demand, with increase in price of a commodity, its demand falls and with decrease in price, its demand increases. Due to this reason, the demand curve of a commodity has a negative slope, as the two variables namely price and quantity demanded, move in opposite direction.

Income demand (change in demand due to change in income)

The income demand differs with the nature of goods.

For *superior goods,* with increase in income of the consumer, the demand increases which means that

there is positive correlation.

As regards the *inferior goods,* the increase in income leads to fall in the demand of these goods, because a consumer, with increase in income starts using superior goods and discards inferior goods. Hence a negative correlation.

As regards the *demand curve,* it shows upward movement from left to right in case of superior goods while downward slope **in** case of inferior goods.

Cross demand (change in demand due to change in price of other commodities)

So far as cross demand is concerned it also has to be seen in the light of complementary goods and substitute goods.

Cross Demand - Complimentary Goods

The complementary goods are those goods which can be used with a particular commodity, such as vehicle and petrol. With increase in price of one commodity, the demand for the complementary commodity will decrease. Due to this reason the demand curve in case of complementary commodity will move from left to right downwards

Cross Demand - Substituted goods

For substitute goods (which can be used in place of another commodity like tea and coffee), with increase in price of one of them, the demand for the substitute commodity will increase. Due to this reason the

demand curve always shows an upward slope from left to right

Different kinds of Goods

a) Superior Goods: There is positive co-relationship between income and demand for superior goods. With increase in income the demand for such goods increases. However, there is negative correlation with price as, with increase in their price, the demand goes down.

b) Inferior goods: These goods are generally the goods for mass consumption such as vanaspati. There is inverse relationship between the demand for inferior goods and increase in income of consumer as the consumers shift their preferences in favour of superior goods with increase in income.

c) Complementary goods: These are the goods that are used with a particular another commodity (for instance the pen and ink, bread and butter). With increase in price of a commodity, the demand of complementary goods decreases along with the demand for the original goods. (say with increase in price of bread, demand for butter goes down).

d) Substitute Goods: These goods are the goods that can be used an alternative to particular goods, such as tea and coffee. In case of increase in the price of particular commodities, the demand for the substitute goods increases because the consumers would give preference to use the alternative goods, available at a lower price.

e) Independent Goods: These are the goods which are not related to each other such as books and clothes. The price change or income change of such goods does not effect the demand for other goods.

GIFFIN GOODS OR GIFFIN PARADOX

Giffin goods are those goods, which are inferior goods compared to the other goods. The concept is related to Sir R. Giffin who stated that the Law of Demand does not become applicable on inferior goods. Demand for such goods increases on increase in their price and decreases when there is decline in their price. This is also called Giffin paradox.

In case of such goods the price effect is positive but the income effect is negative since with increase in income, a consumer starts using the superior goods.

Where does Law of Demand not apply ?

Normally the law of demand explains that the demand of a commodity moves up on decline of its price and vice versa, but in the following situations the law does not apply.

a) Giffin Paradox
b) Commodities which are necessary for life
c) Commodities which involve prestige.
d) High price commodities

e) Emergencies

Reasons for the downward slope to right of demand curve

The demand curve slopes from left to right downwards, because of application of Law of Diminishing Marginal Utility. This law states that with increase in consumption of a commodity by the consumer, each additional unit provides decreased utility.

LAW OF SUPPLY

The law of supply states that the price and supply are directly related as the supply of a commodity increases on increase in its price and it declines, with decline **in** price.

Supply Schedule

The supply schedule can be for an individual firm or can be for the entire market. The supply schedule provides information about different quantities of a commodity, which are offered in a market, for sale, at different prices.

Supply curve - As regards supply curve, it moves from left to right upwards due to positive correlation of supply with price.

Expansion of Supply and Contraction of Supply (due to price factors)

When supply of a commodity increases on account of increase *in price* and declines due to falling price of the commodity, it is called expansion or contraction of supply, respectively. This is also called change in quantity of supply.

Increase in supply I decrease in supply (due to non-price factors)

When supply position of a commodity changes due to a reason *other than the price,* it is called increase in

supply or decrease in supply. The factors other than price, which increase or decrease the supply, include technical changes, change in fashion, social and political factors etc, This is called change in supply

DEMAND SCHEDULE

1. The amount of a commodity people buy depends on its price.
2. The higher the price of an article, other things held constant, the fewer units consumers are willing to buy.
3. The lower is its market price, the more units of it are bought.
4. Other things remaining constant, there is a definite relationship between the market price of a good and the quantity demanded of that good.
5. The relationship between price and quantity bought is called the demand schedule, or the demand curve.
6. The quantity demanded increases with the fall in price.

Demand Curve ; It is a statement depicting the quantity demanded of a commodity at different prices. Demand can be drawn based on demand schedule.

1. The graphical representation of the demand schedule is the demand curve.
2. The quantity demanded is plotted on the horizontal axis (X axis) and the price is plotted on the vertical axis (Y axis).
3. The quantity demanded and price are inversely related.
4. Demand curve slopes downward, going from northwest to southeast. This important property is called the law of downward-sloping demand.
5. *Law of downward-sloping demand:* When the price of a commodity is raised (and other things being constant), buyers tend to buy less of the commodity. Similarly, when the price is lowered, other things being constant, quantity demanded increases.
6. Quantity demand tends to fall as price rises for two reasons. First reason is the substitution effect. When price of a commodity rises, the consumer tries to substitute it with another similar product e.g. Tea and Coffee. Second reason is the income effect when a higher price reduces quantity demanded. When price goes up, one finds himself somewhat poorer than before as effectively real income goes down.

Market Demand:

1. Market demand represents the sum total of all individual demands.
2. The market demand curve is found by adding together the quantities demanded by all individuals at each price.
3. The market demand curve also obeys the law of downward-slopping demand. If prices drop, the lower prices attract new customers through the substitution effect. In addition, a price reduction will induce extra

purchases of goods by existing consumers though both the income and the substitution effects. Conversely, a rise in the price of a good will cause some of us to but less.

Forces behind the Market Demand Curve: Number of factors influences how much will be demanded at a given price: average levels of income, the size of the population, the prices and availability of related goods, individual and social tastes and special influences.

1. The average income of consumers is a key determinant of demand. As people's income rises, individuals tend to buy more of almost everything, even if prices do not change. Automobiles purchases tend to rise sharply with higher levels of income.

2. The size of the market — measured, say, by the population — clearly affects the market demand curve. More the population, more is the demand.

3. The prices and availability of related goods: Demand is affected by availability of substitute products like apples and oatmeal, pens and pencils, small cars and large cars, or oil and natural gas. Demand for good A tends to be low if the price of substitute product B is low.

4. Tastes and preferences: Subjective elements like tastes or preferences also affect demand. Tastes represent a variety of cultural and historical influences. They may reflect genuine psychological or physiological needs (for liquids, love, or excitement). They may also contain a large element of tradition or religion (eating beef is popular in America but taboo in India, while curried jellyfish is a delicacy in Japan but not liked by many Americans.)

5. Special influences: The demand for umbrellas is high in rainy Mumbai but low in sunny Delhi; the demand for air conditioners will rise in hot weather. Further, expectations about future economic conditions, particularly prices, may have an important impact on demand.

SHIFTS IN DEMAND:

1. When there is a change in demand for reasons other than price, it is called Shift in demand curve.
2. Demand curve shifts because factors other than the good's price also change.
3. The net effect on demand due to changes in underlying influences is called an increase in demand.
4. An increase in the demand is indicated by rightward shift in the demand curve and a decrease in demand is indicated by leftward shift in demand curve.
5. The shift in demand means more or less number of commodity will be bought at every price.

THE SUPPLY SCHEDULE:

1. The supply side of a market involves the terms on which businesses produce and sell their products.
2. The supply schedule relates the quantity supplied of a good to its market price, other things being constant.
3. In considering supply, the other things that are held constant include input prices, prices of related goods and government policies.
4. The supply schedule (or supply curve) for a commodity shows the relationship between its market price and the amount of that commodity that producers are willing to produce and sell, other things being constant.
5. Higher the price more supply is expected and lower the price lower would be the supply.

The supply Curve:

1. The supply curve is an upward sloping curve for an individual commodity indicating that as the price of the commodity increases more of it will be produced.
2. One important reason for the upward slope is 'the law of diminishing returns'.

FORCES BEHIND THE SUPPLY CURVE

1. One major factor indicating the forces determining the supply curve, is that producers supply commodities for profit and not for fun or charity.
2. Cost of Production: One major element underlying the supply curve is the *cost of production.* When production costs for a good are low relative to the market price, it is profitable for producers to supply a great deal. When production costs are high relative to price, firms produce little, switch over the production of other products, or may simply go out of business. But production costs are not the only ingredient that goes into the supply curve.
3. Input costs: Production costs are primarily determined by the *price of inputs and technological advances.* The prices of inputs such as labour, energy or machinery obviously have a very important influence on the cost of producing a given level of output.

4: Technological advances: Another important determinant of production costs is *technological advances,* which consist of changes that lower the quantity of inputs needed to produce the same quantity of output. Such technological advances include scientific breakthroughs, better application of existing technology, reorganization of the flow of work.

5. Price of related goods: Supply is also influenced by the *prices of related-goods,* particularly goods that are alternative outputs of the production process. If the price of one production substitute rises, the supply of another substitute will decrease.

6. Government policy also has an important influence on the supply curve. Environmental and health considerations determine that technologies can be used, while taxes and minimum-wage laws can significantly raise input prices.

7. Special factors:. The weather exerts an important influence on farming and on the agro-industry. The computer industry has been marked by a keen spirit of innovation, which has led to a continuous flow of newer products. Market structure will affect supply, and expectations about future prices often have an important impact upon supply decisions.

SHIFTS IN SUPPLY

1. When changes in factors other than a good's own price affect the quantity supplied, it is called as shifts in supply. Supply increases (or decreases) when the amount supplied increases (or decreases) at each market price.

EQUILIBRIUM OF SUPPLY AND DEMAND

1 Supply and demand interacts to produce an equilibrium price and quantity or market equilibrium. .

2. The market equilibrium comes at that price and quantity where the forces of supply and demand are in balance. At the equilibrium price, the amount that buyers want to buy is just equal to the amount that sellers want to sell.

3. It is called equilibrium because when the forces of supply and demand are in balance, there is no reason for price to rise or fall, as long as other things remain unchanged.

4. A market equilibrium comes at the price at which quantity demanded equals quantity supplied. At that equilibrium, there is no tendency for the price to rise or fall.

5. The equilibrium price is also called the market-clearing price. This denotes that **all** supply and demand orders are filled, the books are 'cleared' of orders and demander's and suppliers are satisfied.

Equilibrium with Supply and Demand Curves

1. The market equilibrium is for the price at which quantity demanded equals quantity supplied. The equilibrium price comes at the intersection of the supply and demand curves.

2. The equilibrium price and quantity come where the amount willingly supplied equals the amount willingly demanded. In a competitive market, this equilibrium is found at the intersection of the supply and demand curves. There are no shortages or surpluses at the equilibrium price.

EFFECT OF A SHIFT IN SUPPLY OR DEMAND

1. The supply-and-demand curves can be used to ascertain the equilibrium price and quantity.
2. It can also be used to predict the impact of changes in economic conditions on prices and quantities.
3. For example, if due to bad weather the price of wheat increases which is a key ingredient of bread. That shifts the supply curve for bread to the left. But, the demand curve for bread does not shift because people's sandwich demand is largely unaffected by farming weather. However, if prices do not change, then due to increase in price of input, bakers will produce less bread at the old price. So quantity demanded exceeds quantity supplied. The price of bread therefore rises, encouraging production and thereby raising quantity supplied, while simultaneously discouraging consumption and lowering quantity demanded. The price continues to rise until, at the new equilibrium price, the amount demanded and supplied are once again equal.
4. The supply-and-demand curves can also be used to examine how changes in demand affect the market equilibrium. For example, with a sharp increase in family incomes, everyone wants to eat more bread resulting in a 'demand shift' rightward. The demand shift produces a shortage of bread at the old price. Prices are raised until supply and demand come back into balance at a higher price.

MONEY SUPPLY AND INFLATION

WHAT IS MONEY

Money is anything which performs the following functions (I) Medium of Exchange; (ii) A measure of value; (iii) A store of value over time; (iv) Standard for deferred payments;

1. Medium of Exchange: Individual goods and services, and other physical assets, are 'priced' in terms of money and are exchanged using money.
2. A Measure of Value: Money is used to measure and record the value of goods or services.
3. A store of value over time: Money can be held over a period of time and used to finance future payments.
4. Standard **for** Deferred Payments: Money is used as an agreed measure of future receipts and payments in contracts.

MONEY SUPPLY:

1. Money supply refers to the stock of money in circulation in the economy at a given point of time.
2. This is partly exogenous (decided by the government and the central bank) and partly endogenous.

Measures of Money Supply

Money stock measures were introduced by RBI during 1970 and the working group under Y B Reddy suggested major changes in the money stock measures, which gave its recommendations (during Dec 1997) and implemented during June 1998. The current measures are monetary (M) and liquidity (L) aggregates.

1. M 0: (weekly report): Currency in circulation + Bankers' deposits with RBI + Other deposits with RBI (including primary dealers' balance).
2. M 1:-(Narrow money) : fortnightly report: Currency with public + Current deposits with banking system + 15% **of** demand liabilities portion of saving deposits with banking system + Other deposits with RBI.
3. **M** 2: fortnightly report: M **1+** Time liabilities portion (i.e. remaining 85%) of saving deposits with banking system + Certificates of deposits issued by banks + Term deposits (excluding FCNR-B deposits) with a contractual maturity of up to and including one year with banking system.
4. M 3: (Broad money) fortnightly report: M 2 + Term deposits (excluding FCNR-B) with a contractual maturity of over one year with the banking system + Call borrowings from non-depository financial corporations by the banking system.

Important points regarding monetary aggregates:

1.M0 is essentially the monetary base, compiled from the balance sheet of RBI.

2. **M1** purely reflects the non-interest bearing monetary liabilities of banking system.
3. **M 2,** besides currency and current deposits, includes saving and short term deposits reflecting the transactions balances of entities.
4. **M3** has been redefined to reflect, in addition to M2, the call funding that the banking systems obtains from other financial institutions.

Liquidity Aggregates

1. **L 1 =** M 3 + all deposits with post office saving banks (excluding NSCs), **L2 = L** 1 + term deposits with term lending institutions and refinancing institutions (FIs) + term borrowin *by FIs + certificate of deposits issued by FIs and **L 3 = L** 2 + public deposits of NBFCs.

INFLATION

Inflation refers to regular increase in the general price level of prices of goods and services, in an economy, over a period of time. Inflation leads to fall in purchasing power,' because with rise in price of goods and services, the same amount of money, can purchase fewer goods and services.

Inflation has positive as well as negative impact on the economy. Inflation helps in bringing an economy out of recession. The negative effect is loss in real value of money.

1. Inflation refers to a sustained rise in the general level of prices of goods and services in an economy over a period of time.
2. Inflation leads to fall in purchasing power. When the price level rises, each units of currency buys fewer goods and services; consequently, inflation is also erosion in the purchasing power of money a loss of real value in **the** internal medium of exchange and unit of account in the economy.
3. Measure of price inflation is the inflation rate, i.e. the annualized percentage change in a general price index over time.

4. Inflation has both positive and negative effects on an economy. Negative effects of inflation include loss in stability in the real value of money and other monetary items over time, uncertainty about future inflation may discourage investment and saving, and high inflation may lead to shortages of goods if consumers begin hoarding out of concern that prices will increase further in the future. Positive effects include a mitigation of economic recessions and debt relief by reducing the real level of debt.

TYPES OF INFLATION

Demand-Pull Inflation: It is rise in general prices caused by increasing aggregate demand for good and services. Increasing quantity of money in the hands of the people increases the aggregate demand for goods and services, and if aggregate supply does not follow the suit, prices rise.

Cost — Push Inflation: It is a type of inflation caused by substantial increases in the cost of production of important goods or services where no suitable alternative is available. For example, if prices of some key inputs like oil rise, producers will have to either adjust output supply or translate the higher costs into higher output prices. When output declines because of cost pressure on producers, there will be a shortage in output markets and as a result prices will rise.

MEASURES OF INFLATION: Inflation denotes a rise in the general level of prices. The general price level is measured by a price index. A price index is a weighted average of the prices of a selected basket of goods and services relative to their prices in some designated base-year.

Calculating Inflation with Price Indexes Inflation is calculated by taking the price index of the year for which inflation is being measured and subtracting the base year from it, then dividing by the base year. This is then multiplied by 100 to give the percentage(%) change in inflation.

Inflation = (Price Index in Current Year — Price Index in Base Year)/ Price Index in Base Year*100

The most important price indexes are: (i) Wholesale Price Index (WPI) (ii) Food Inflation Index (iii) Consumer Price Index (CPI) (iv) GDP deflator

Wholesale Price Index (WPI): The WPI reflects the change in the level of prices of a basket of goods at the wholesale level. WPI focuses on the price of goods traded between corporations at the wholesale stage, rather than goods bought by consumers. WPI helps to monitor price movements that reflect supply and demand in industry, manufacturing and construction sectors. It is called Headline inflation.

Food Inflation index Recently, it has been decided by government that WPI will be announced monthly. However the indices for the food group and fuel group will be announced weekly.

Consumer Price Index (CPI) The CPI reflects the change in the level of prices of a basket of goods and services purchased/consumed by the households. It measures the prices at the retail level. This is the measure of inflation more relevant for the consumers. It is the cost of living index popularly known as Core Inflation. There are four different index numbers of consumer prices. These are: (i) CPI for industrial workers (CPI-1W) (ii) CPI for agricultural labourers (CPI-AL) (iii) CPI for rural workers (CPI-RW) and (iv) CPI for urban non-manual employees (CPI-UNME). CP! in India is released by Labour Bureau, Ministry of Labour and Employment, Government of India.

GDP Deflator GDP deflator is a measure of the level of prices of all new, domestically produced, final goods and services in an economy. The GDP deflator is not based on a fixed basket of goods and services. The basket is allowed to change with people's consumption and investment patterns.

INFLATION & RELATED ISSUES

For a common man, inflation stands for an increase in prices. To reflect the change in prices of various commodities, a price index is constructed. This index captures the overall rate of price change assigning different weights to different items.

Different price indices: There are 5 different price indices for different groups of people as different people are affected differently by the price change. These indices include wholesale price index (WPI), consumer price index for agricultural labour (CPI-AL), consumer price index for industrial workers (CPI-1W), consumer price index for urban non-manual employees (CPI-UN ME)and consumer price index for rural labour (CPI-RL).

WPI measures the changes in wholesale prices. Normally, the inflation rate is expressed through wholesale price index. The change in the index for a particular week shows as to how the average level of prices of

different commodities included in the WPI has changed in comparison to the corresponding week, a year ago. Whenever the rate increases it is indicator of increase in prices and whenever there is decrease, it does not necessarily mean the decrease in prices. Rather it may indicate, lower rate of increase in prices. The official inflation rate is announced in the form of WPI.

Indices for groups of consumers: WPI does not reflect the change in prices concerning a particular group of consumers. This aspect is taken care of by other indices i.e. CPI-AL, CPI-1W, CPI-UNME and CPI-RL. These indices take into account the prices of commodities, that affect the consumption pattern of a particular group.

Causes for the current inflation rate: The present high inflation rate is the result of increase in the prices of various commodities (such as pulses, fruits, vegetables, basic metal, cement, edible oils etc.). Inflation was placed at 6.73% as on Feb 03 on WPI basis. For agricultural labour (CPI-AL) was 8.93% for the same period.

Why normal prices are higher than official inflation : The price paid by the consumer for various commodities is reflected in consumer price index. The goods used by the consumers such as wheat, pulses and fruits, have higher weightage in consumer indices when compared to the WPI. In the wholesale index, the prices of all commodities are taken into account (where the weightage of individual items included in CPI is low) due to which it reflects a different price level.

Effect of inflation : Inflation affects the common man having lower purchasing power, more than the well to do persons having higher purchasing power. This reduces the real income of the consumer and the consumer is made to pay more for same quantity of goods. With an increasing inflation rate, there is increase in general interest rates on deposits/advances, which increases cost of production and sale of various goods and leads to further increase in inflation.

Inflation and money supply expansion : The money supply expansion (M3) has direct relationship with the change in inflation rate. The higher money supply expansion leads to increase in inflation rate because the liquidity fuels increase in prices of various commodities for various reasons. To control money supply expansion, RBI has to increase indicator rates such as Bank rate and Repo Rate.

How govt. and RBI control inflation : The govt. takes *non-monetary initiatives* relating to demand and supply side of the real market such as restriction on exports of certain commodities, liberalization of import of essential commodities by cutting down custom duties, steps to increase the production of goods and services, check hoarding etc. RBI initiates monetary measures to check inflation that include curbing the liquidity by increase in statutory reserve requirements i.e. cash reserve ratio and statutory reserve ratio that divert the use of bank deposits from loans and advances to cash and govt. securities. RBI in order to discourage banks from undertaking loans to unproductive sectors of the economy also increases the risk weightage for capital adequacy and provisioning requirements in case of standard assets for such loans.

INFLATION & RELATED TERMS

1. **Inflation:** A situation of a steady and sustained rise in general prices is usually known as inflation. Inflation is a state in which the value of money is falling i.e. prices are rising.
2. **Cost-push Inflation:** It arises due to an increase in production cost. Such type of inflation is caused by three factors: (i) an increase in wages, (ii) an increase in the profit margin and (iii) imposition of heavy taxation.
3. **Demand- push Inflation**: It arises as a result of strong consumer demand. When many individuals are trying to purchase the same good, the price will inevitably increase. When this happens across the entire economy for all goods, it is known as demand-pull inflation
4. **Deflation:** Deflation is the reverse case of inflation. Deflation is that state of falling prices which occurs at that time when the output of goods and services increases more rapidly than the volume of money in the economy. In the deflation the general price level falls and the value of money rises.
5. **Disinflation:** A fall in the rate of inflation. This means a slower increase in prices but not a fall in prices
6. **Recession**: A period of slow or negative economic growth, usually accompanied by rising unemployment.
7. **Stagnation:** A prolonged recession, but not as severe as a depression.

8. **Disinflation:** A fall in the rate of inflation. This means a slower increase in prices but not a fall in prices.
9. **Depression:** A prolonged recession in economic activity. The textbook definition of a recession is two consecutive quarters of declining outpur. A depression is an even deeper and more prolonged slump.

THEORIES OF INTEREST

What is Interest: There are four types of income i.e. rent, wages, interest, profit. Interest is paid for use of capital and it may be gross interest or net interest.

As per Marshall, 'Interest is the price for the use of capital in a market'. In other words, interest is that part of national income which is paid to capitalists as a reward of the services of capital. However, in Keynes opinion, interest is a reward for parting with liquidity for a specified period.

Three distinct elements can be distinguished in interest:

a) Reward for the risk involved in making the loan;

b) Payment for the trouble involved;

c) Pure interest, i.e., price of the capital.

Gross interest is the payment which the borrower makes to the lenders for use of money. **It** includes not only the net interest but reward for risk, inconvenience, pains and management.

GROSS INTEREST = Net interest + reward for risk + reward for inconvenience + reward for pains + reward for management.

Net interest on the other hand is the payment for using the capital only and does not include other elements mentioned as above.

NET INTEREST = (Gross Interest) — (Reward for Risk + Reward for inconvenience + Reward for Pains + reward for management).

Features of interest:

(i) payment for the risk involved in making the loan;
(ii) payment for the trouble involved;
(iii) pure interest, that is a payment for the use of the money.

1 At any particular time-there is a prevailing rate of interest, which many regard as a price determined like other prices in markets, by the demand to borrow in relation to the supply of loanable funds. This is pure interest.

2. Differences in the rate of interest on different loans made during the same period of time must, therefore, be due to differences in the risk or trouble involved. Thus, the rate of interest charged by a moneylender on an unsecured loan will be higher than the rate charged by a bank to one of its customers who can offer satisfactory collateral security. Similarly, the government has generally to offer a higher rate of interest on a long-term than on a short-term loan.

FACTORS AFFECTING THE RATE OF INTEREST:

a) Difference is risk perception.
b) Difference on account of credit rating of borrower.
c) Difference in maturity period of loan.
d) Purpose and end use of the loan.
f) Nature of the primary and collateral security.
g) Quality of third party guarantee.

IMPORTANT THEORIES OF INTEREST

A) Prof. Senior: Abstinence theory of Interest: "Interest is the reward for waiting and abstinence".

B) Fishers Time Preference Theory of Interest: Interest is the reward paid to induce people to postpone their present consumption and to lend their money.

C) Keynes Liquidity Preference Theory of Interest: Prof J.M. Keynes in his book, the General Theory of Employment, Interest and Money, has viewed rate of interest as a purely monetary phenomenon and is determined by demard for money and supply of money. According to this theory, rate of interest is determined by liquidity preference, i.e., demand of money on one side and the supply of money on the other. Demand of money means the demand for keeping money in liquid form. Thus, demand of money

means liquidity preference. The term liquidity preference means the habit cf persons to keep their money in liquid form. When a person gets his income, he has to take two important decisions:

a) How much to spend and how much to save, and
b) How much to save in liquid form and how much to save in non-liquid form.

The term liquid form means to keep money in the form of ready purchasing power i.e. cash or gold or any such way as can readily be converted into cash. The term non-liquid form means to invest money in iong term securities and capital goods

FACTORS AFFECTING LIQUIDITY PREFERENCE

Keynes explained interest in terms of purely monetary forces. Keynes assumed a simplified economy where there are two assets which people can keep in their portfolio balance. These two assets are:

a) Money in the form of currency and current deposits in the banks which earn no interest,
b) According to Keynes, rate of interest and bond prices are inversely rlated. When bondprices go up, rate of interest rises and vice versa. The demand for money by the people depends upon how they decide to balance their portfolios between money and bonds. This decision about portfolio bal?nre ran he influenced by two factors.

First, the higher the level of nominal income in a two-asset economy, more the money people would want to hold in their portfolio balance. This is because of transactions motive according to which at the higher level of nominal income, the purchases by the people of goods and services in their daily life will be relatively larger, which require more money to be kept for transactions purposes.

Second, the higher the nominal rate of interest, the lower the demand for money for speculative motive. This is firstly because a higher nominal rate of interest implies a higher opportunity cost for holding money. At higher rate of interest, holders of money can earn more incomes by holding bonds instead of money. Secondly, if the current rate of interest is higher than what is expected in the future, the, people would like to hold more bonds and less money in their portfolio. On the other hand, if the current rate of interest is low (in other words, if the bond prices are currently high), the people will be reluctant to hold larger quantity of bonds (and instead they could hold more money in their portfolio) because of the inherent fear that bond prices would ne fall in the future causing capital losses to them.

Prof. Keynes cites three motives to explain why people prefer to keep their money in liquid form. These motives are as under **1.Transactional Motives**: People keep a part of their income in liquid form so that they can pay their regular expenses. Liquidity preference for transactional motives will depend upon the size of income, time of receipt and number of transactions.

2.Precautionary Motives: People keep some part of income to provide for contingencies, such as illness, accident, unemployment etc. Liquidity preference for such motives depends upon the level of income, size of family, living conditions and habit of individuals etc. **3.Speculative Motives**: Some persons like to keep their money in liquid form for speculative purposes also so that they can get the advantage of changes in the rate of interest.Thus, **Demand of money = Transactional motive + Precautionary motive + Speculative motive.**

Liquidity preference depends upon the income and rate of interest. There is an inverse relationship between rate of interest and demand for money (liquidity preference). If the rate of interest is high, liquidity preference will be less because the people would like to invest more and more amount. If the rate of interest is low, liquidity preference will be more because the people would like to keep the money with themselves.

Other theory of Interest

Marginal Productivity theory: According to this theory, interest is paid because capital helps in production. The borrower can earn more, by using the capital. Since law of diminishing returns applies on production, the interest rate is determined by the marginal productivity of capital.

Loanable Funds Theory: According to this theory, propounded by a number of economists, the rate of interest is determined by demand and supply of loanable funds. As per the theory, interest is the price paid for use of loanable funds and it is fixed at a point, at which demand and supply are equal.

Keynes's Liquidity Preference Theory: '

1. The rate of interest is a purely monetary phenomenon and is determined by demand for money and

supply of money. The theory is known as Liquidity Preference Theory.

2. According to Keynes, demand for money means demand for keeping funds in liquid form i.e. liquidity preference.

3. According to the theory, it is natural tendency to keep savings in liquid form to the extent possible but the liquidity can be parted with for certain period. To part with the liquidity for such certain period, the interest is the reward.

4. The demand for money may arise for a number of reasons i.e. transaction motives (day to day expenses), precautionary motives (against possibility of sudden need say for health), and speculative motive (to take advantage of possible gains).

5. The rate of interest is determined at the that point where demand and supply are equal, which is determined by liquidity preference.

The Demand for Money in a Two-Asset Economy: According to Keynes, people can keep two types of assets in their portfolio balance. These two assets are: (1) money in the form of currency and current deposits in the banks which earn no interest, (2) long-term bonds. The decision of people to balance their portfolios between money and bonds is influenced by two factors.

1. Level of nominal income: Higher the level of nominal income in a two-asset economy, more the money people would want to hold their portfolio balance. This is because of transaction motive according to which at the higher level of nominal income, the people will purchase more of goods and services in their daily life, which require more money to be kept for transactions purposes.

2. Nominal rate of interest: Higher the nominal rate of interest, the lower the demand for money for speculative motive because a higher nominal rate of interest implies a higher opportunity cost for holding money. At higher rate of interest, holders of money can earn more incomes by holding bonds instead of money. Secondly, if the current rate of interest is higher than what is expected in the future, the people would like to hold more bonds and less money in their portfolio. On the other hand, if the current rate of interest is low (in other words, if the bond prices are currently high), the people will be reluctant to hold larger quantity of bonds (and instead they could hold more money in their portfolio) because of the inherent fear that bond prices would fall in the future causing capital losses to them. { It may be noted that rate of interest and bond prices are inversely related. When bond prices go up, rate of interest rises and vice versa.}

MONEY DEMAND CURVE:

1. Quantity of money demanded increases with the fall in the rate of interest or with the increase in level of nominal income.

2. At a given level of nominal income, a money demand curve can be drawn showing the quantity of money demanded at various rates of interest.

3. As demand for money is inversely related to the rate of interest, the money demand curve at a given level of income, will be downward-sloping.

4. When the level of money income increases, the curve of demand for money shifts upward.

DETERMINATION OF RATE OF INTEREST : EQUILIBRIUM IN THE MONEY MARKET

According to Keynes, the rate of interest, is determined by demand for money (Liquidity Preference) and supply of money. The factors which determine demand for money has been explained above. The supply of money, at a given time, is fixed by the monetary authority of the country.

1. Money supply curve is represented by a vertical straight line parallel to Y axis.

2. The money market is in equilibrium at a interest rate at which Demand curve intersects supply curve.

3. At higher than equilibrium rate, supply of money exceeds the demand for money. The excess supply of money reflects the fact that people do not want to hold as much money in their portfolio as the monetary authority has made it available to them. In such situation, the people holding assets in money form would buy bonds and thus replace some of money in their portfolio with bonds. Since the total money supply at a given moment remains fixed, it cannot be reduced by buying bonds by individuals. Such bonds-buying spree would lead to the rise in prices of bondS. The rise in bond prices mean the fall in the rate of interest. With the fall in the interest rate, quantity demanded **of** money become once again equal to the given supply of money, and the excess supply of money is entirely eliminated and money market is in equilibrium.

4. On the other hand, if the rate of interest is lower than the equilibrium rate, there will be excess demand

for money. As a reaction to this excess demand for money, people would like to sell bonds in order to obtain a greater of money for holding at lower rate of interest. The stock of money remaining fiXed, the attempt by the people to hold more money balances at a rate of interest lower than the equilibrium level through sale of bonds will only cause the bond prices to fall. The fall in bond prices implies the rise in the rate of interest.
Thus, the process that started as a reaction to the excess demand for money at an interest rate below the equilibrium will end up with the rise in the interest rate of the equilibrium level.

EFFECT OF AN INCREASE IN THE MONEY SUPPLY ON INTEREST RATE

1. Rate of interest will be determined where the demand for money is in balance or equal to the fixed supply of money.
2. Assuming no change in expectations and nominal income, an increase in the quantity of money (through buying securities by the central bank of the country from the open market), will lower the rate of interest.
3. If money supply is expanded, there emerges excess supply of money at the initial rate of interest. The people would react to this excess quantity of money supplied by buying bonds. As a result, the bond prices will go up which implies that the rate of interest decline. This is how the increase in money supply leads to the fall in rate of interest.

SHIFTS IN MONEY DEMAND OR LIQUIDITY PREFERENCE CURVE:

1. The position of money demand curve depends upon two factors: (1) the level of nominal income and (2) the expectations about the changes in bond prices in the future which implies change in interest in future.
2. A money demand curve is drawn by assuming a certain level of nominal income. With the increase in nominal income, money demand for transactions and precautionary motives increase causing an upward shift in the money demand curve.
3. **Shifts in money demand curve** (or what Keynes called liquidity preference curve) can also be caused by changes in the expectations of the people regarding changes in bond prices or movements in the rate of interest in future. If some changes **in** events lead the people to expect a higher rate of interest in the future than they had previously supposed, the money demand or liquidity preference for speculative motive will increase which will bring about an upward shift in the money demand curve or liquidity preference curve and this will raise the rate of interest.

MODERN THEORY: HICKS — HANSEN SYNTHESIS: IS-LM CURVE MODEL

1. Modern theory was propounded by Hicks and Hensen.
2. According to the theory, the interest depends upon saving, investment, liquidity preference and income.
3. The rate of interest according to the theory is determined by monetary equilibrium and income equilibrium.
4. This theory is a synthesis between the Classical and Keynes' theories of interest.
5. **It** has propounded an adequate and determinate theory of interest through the intersection of what are called IS and LM curves.
6. According to Hicks and Hansen, the classical and loanable funds theories amount to the same thing. The difference between these two theories, i.e. classical and loanable funds, lies only in the meaning of savings.
7. IS curve is derived from various saving curves at various income levels together with the given investment demand curve. This IS curve tells us what will be the various rates of interest at different levels of income, given the investment demand curve and a family of saving curves at different levels of income.
8. LM curve is obtained from Keynes' formulation. The LM curve is obtained from a family of liquidity preference curves corresponding to various income levels together with the given stock of money supply. This is because as the level of income increases, people would like to hold more money under the transactions motive. That is, the higher the level of income, the higher would be the liquidity preference curve. With the given supply of money, the different levels of liquidity preference curves corresponding to various levels of income would determine different rates of interest. This yields LM curve, which depicts the various combinations of interest and income level, at which money market is in equilibrium.
9. Hicks and Hansen show that with the intersection of IS and LM curves, both the interest and income are simultaneously determined. Thus the classical and Keynes' theories taken together help us in obtaining as adequate and determinate theory of interest.

DERIVATION OF THE IS CURVE:

1 As the income rises, the savings curve shifts to the right and the rate of interest, which equalizes savings and investment, falls.

2. Since, as income increases, rate of interest falls, the IS curve slopes downward.

3. IS curve relates the rates of interest with the levels of income at which intended savings and investment are equal. In other words, the IS curve depicts the various combinations of levels of interest and income at which, intended savings equal investment; goods-market is in equilibrium.

4. Since with the increase in income the savings curve shifts to the right, its intersection with the investment demand curve will lower the rate of interest.

5. The level of income and rate of interest are inversely related. That is, the **IS** curve slopes downward.

6. Further, the steepness of the IS curve depends upon the elasticity or sensitiveness of investment demand to the changes in rate of interest. A given change in interest will produce a large change in investment and thereby cause a large change in the level of income.

7. Thus when investment demand is greatly elastic or highly sensitive to the rate of interest, the IS curve will be flat (i.e. less steep). On the other hand, when investment demand is not very sensitive to the changes in rate of interest, the IS curve will be relatively steep.

8. The *position of IS curve and changes in its level are determined by the level of autonomous expenditure

such as government expenditure, transfer payments, autonomous investment. If the government expenditure or any other type of autonomous expenditure increases, it will increase the equilibrium level of income at the given rate of interest. This will cause the IS curve to shift to the right. A reduction in government expenditure or transfer payments will shift the IS curve to the left.

DERIVATION OF THE LM CURVE FROM KEYNES' LIQUIDITY PREFERENCE THEORY

1. The LM curve can be derived from the Keynesian liquidity preference theory of interest.

2. Liquidity preference or demand for money to hold depends upon transaction motive and speculative motive.

3. It is the money held for transactions motive which is a function of income. The greater the level of income, the greater the amount of money held for transactions motive and, therefore, the higher the level of liquidity preference curve.

4. A family of liquidity preference curves can be drawn at various levels of income. The intersection of these various liquidity preference curves, corresponding to different income levels with the supply curve of money fixed by the monetary authority, would give the LM curve that relates the rate of interest with the level of income as determined by money-market equilibrium corresponding to different levels of liquidity preference curve.

5. The LM curve tells us what the various rates of interest will be (given the quantity of money and the family of liquidity preference curves) at different levels of income. But the liquidity preference curves alone cannot tell us what exactly the rate of interest will be.

6. As income increases, liquidity preference curve shifts outward and therefore the rate of interest, which equates supply of money with demand for money, rises.

THE SLOPE AND POSITION OF THE LM CURVE

1. The LM curve slopes upward to the right. This is because with higher levels of income, demand for money (that is, the liquidity preference curve) is higher and consequently the money-market equilibrium, that is, the equality of the given money supply with liquidity preference curve occurs at a higher rate of interest. This implies that rate of interest varies directly with income

2. Factors that determine the slope of the LM curve include (i) Responsiveness of demand for money (i.e. Liquidity Preference) to the changes in income and (ii) Elasticity or responsiveness of demand for money (i.e., liquidity preference for speculative motive) to the changes in rate of interest.

3. As the income increases, demand for money would increase for being for transactions motive. This extra demand for money would disturb the money-market equilibrium, and in order to restore the equilibrium the rate of interest will rise to the level where the given money supply curve intersects the new liquidity preference curve corresponding to the higher income level.

4. In the new equilibrium position, with the given stock of money supply, money held under the transactions motive will increase whereas the money held for speculative motive will decline. The greater the extent to which demand for money for transaction motive increases with the increase in income, the greater the decline in the supply of money available for speculative motive.

5. Given the liquidity preference schedule for speculative motive, the higher the rise in the rate of interest, the steeper the LM curve consequently.
6. According to Keynes' liquidity preference theory, r = *f* (M2,L2) where M2 is the stock of money available for speculative motive and L2 is the money demand or liquidity preference function for speculative motive.
7. The second factor which determines the slope of the LM curve is the elasticity or responsiveness of demand for money (i.e., liquidity preference for speculative motive) to the changes in rate of interest. The lower the elasticity of liquidity preference with respect to the changes in interest rate, the steeper will be LM curve.
8. On the other hand, if the elasticity of liquidity preference (money-demand function) to the changes in the rate of interest is high, the LM curve will be relatively flat or less steep.

What brings about shifts in the LM curve?:

1. An LM curve is drawn with a given stock of money supply. Therefore, when the money supply increases, given the liquidity preference function, it will lower the rate of interest at the given level of income. This will cause the LM curve to shift down and to the right. On the other hand, if money supply is reduced, given the liquidity preference (money; demand) function, it will raise the rate of interest at the given level of income and therefore cause the LM curve to shift above and to the left.
2. The other factor that causes a shift in the LM curve is the change in liquidity preference (money demand function) for a given level of income. If the liquidity preference function for a given level of income shifts upward, this, given the stock of money, will lead to the rise in the rate of interest. This will bring about a shift in the LM curve above and to the left. On the contrary, if the liquidity preference function for a given level of income declines, it will lower the rate of interest and will shift the LM curve down and to the right.

Intersection of the IS and LM curves: Simultaneous determination of interest rate and income

1. The IS curve and the LM curve relate the two variables: (a) income, and (b) the rate of interest.
2. Income and the rate of Interest determined together at the equilibrium rate of interest are, at the point of intersection of IS and LM curve.
3. At this point, income and the rate interest stand in relation to each other such that (1) investment and saving are in equilibrium, and (2) the demand for money is in equilibrium with the supply of money (Le., the

desired amount of money is equal to the actual supply of money).
4. Thus, a determinate theory of interest is based on: (1) the investment-demand function, (2) the saving function (or, conversely, the consumption function), (3) the liquidity preference function, and (4) the quantity of money.
5. According to Hicks and Hansen, both monetary and real factors, namely, productivity, thrift, and the monetary factors, that is, the demand for money (liquidity preference) and supply of money play a part in determining of the rate of interest. Any change in these factors will cause shift in IS or LM curve and will therefore change the equilibrium level of the rate of interest and income.

BUSINESS CYCLES

Business cycle or economic cycle

The business cycle is the periodic but irregular up-and-down movements in economic activity, measured by fluctuations in real GDP and other macroeconomic variables. In other words, a business cycle or an economic cycle refers to economy-wide fluctuations in economic activity (including production of goods and services), over several months or years. Such cycle pass through phases of prosperity and depression. A business cycle is not predictable, regular or repetitive. Its timing is random and unpredictable. The business cycles influence the business decisions and lead to impact on individual firms and the economy as a whole. Characteristics of a business cycle: It is synchronic: The upward or downward movement tend to occur almost at the same time, in all industries. Prosperity or depression in one industry will have impact in other industries, almost immediately. It shows a wave-like movement: The period of boom and depression comes alternatively. Cyclical fluctuations are recurring in nature: Various phases are repeated. A boom is followed by depression which is followed by prosperity again.
Downward movements are more sudden, than the upward movements There is no indefinite depression or boom period. Phases of a business cycle A business cycle has 4 phases namely (i) Boom (2) Recession (3) Depression (4) recovery

Business Cycle or Trade Cycle

1. The term **business cycle** (or economic cycle) refers to economy-wide fluctuations **in** production or economic activity over several months or years. These fluctuations occur around a long-term growth trend, and typically 'involve shifts over time between periods of relatively rapid economic growth (expansion or boom), and periods of relative stagnation or decline (contraction or recession).
2. Business cycle simply means the whole course of business activity which passes through the phases of prosperity and depression. A business cycle is not a Tegular, predictable, or repetitive phenomenon like the swing of the pendulum of a clock. lts timing is random and, to a large degree, unpredictable.
3. The business cycles influence business decisions. The cycles affect not only the economy in general, but each individual business firm.

Characteristics of a Business Cycle:

1. A business cycle is synchronic. The upward and downward movements tend to occur at almost the same period in all industries. The wave of prosperity or depression in one industry will soon generate a wave in other industries.

2. A business cycle shows a wave-like movement. The period of prosperity and depression can be alternatively seen in a cycle.

3. Cyclical fluctuations are recurring in nature. The various phases are repeated. A boom Is followed by depression and the depression again is followed by boom.

4. There can be no indefinite depression or eternal boom period.
5. Business cycles are pervasive in their effects.
6. The up and down movements are not symmetrical. The downward movement is more sudden and violent than the upward movement.

Phases of a Business Cycle: A business cycle is identified as a sequence of four phases, viz., recovery, boom, recession and depression.

Boom:

1. During the boom phase, production capacity is fully utilized and also products fetch an above-normal price which gives higher profit.
2. This attracts more and more investors. To manufacture more number of products entrepreneur purchases new machines and also employees work at higher wage rate.
3. The increasing cost tendency of the factors of production leads to a continuous increase in product cost.
4. The fixed income group or the salaried class finds it difficult to cope with this increase in prices. As their income does not increase accordingly, they are now compelled to reduce their consumption. The demand is now more or less stagnant or it even decreases. Thus the boom or prosperity reaches its peak.

Recession:

1. Once economy reaches the peak the course changes. A downward tendency in demand is observed.
2. The producers who are not aware of this trend go on producing. The supply now exceeds demand.
3. **The** producers come to notice that their stocks are piling up. They are compelled to give up future investment plans. The order for new equipments and raw materials are cancelled. A businessman even cuts down his existing business.
4. Workers are retrenched.
5. Bankers insist on repayment, stocks accumulate, business failure increases, investment ceases and unemployment expands.

. Unemployment leads to fall in income, expenditure, prices, profits and industrial and trade activities.

Desire for liquidity increases all around. Producers are compelled to reduce price so that they can find money to meet their obligations. Consumers who expect a still further decline in prices postpone their consumption. Stocks go on piling up. Some firms are forced into bankruptcy. The failure of one firm affects other firms with whom it has business connections. There is general distress. This phase of the business cycle is known as the crisis. It is the utmost suffering for a business.

Depression:

1. Under employment of both men and materials is a characteristic of this phase.
2. General demand falls faster than production.
3. Producers are compelled to sell their goods at a price which will not even cover the full cost.
4. Manufacturers of both capital goods and consumers goods are forced to reduce the volume of production. As a consequence, workers are thrown out. The remaining workers are poorly paid.
5. The demand for bank credit is at its lowest which results in idle funds. The interest rates also decline.
6. The firms that cannot pay off their debts are wound up. Prices of shares and securities fall down. Pessimism prevails in the economy. The less-confident investors are not ready to take up new investment projects. The aggregate economic activity is at its bottom.

Recovery

Depression phase does not continue indefinitely. Depression contains in itself the germs of recovery. The idle workers now come forward to work at low wages. As the prices are at their lowest, the consumers, who postponed their consumption expecting a still further fall in price, now start consuming. The banks, with accumulated cash reserves, now come forward to give loans at easier terms and lower rates. As the demand increases, the stocks of goods become insufficient. The economic activity now starts picking up, investment picks up, and employment and output slowly and steadily begin to rise. Increased income leads to increase in demand, resulting in rise in prices, profits, further investment, employment and incomes. The wave of recovery once initiated--soon begins to feed upon itself. Stock markets become alive thus hastening the revival. Optimism develops among the entrepreneurs. Bank loans and demand for credit start rising. The depression phase then gives way to recovery.

INDIAN ECONOMY

Salient features of Indian economy

Dominance of agriculture and heavy population pressure on agriculture: Per capita land availability is very low and per hectare labour use is very high. **Agriculture** sector provides livelihood tc about 65% of Indian population, while the share of **agriculture** to GDP **is around** 17%.

Low per capita income : According to World Development Report 2007, India's **per** capita income was US $ 95o (as a result India falls in Middle Economies). It is **1/5oth of US** per capita income.

Disparities in income distribution : As per NSSO data, 39% of rural **population** possesses only 5% of all rural assets while, 8% top households possess 46% of total **rural** assets. This shows high degree of disparity in income and wealth distribution. **Over-population : India** is over-populated country, next only to China with **total** population of about 12o cr. To maintain 16.7% of world's population, India holds **only** 2.42% of total land area of the world.

Unbalanced economic development : As per World Development Report 2007, 64% of total labour force depends on agriculture, 16% on industry and about 2o% on trade, transport and other services.

Lack of capital : Due to low per capita income, the savings are low in India, though in the recent years, some improvement has been observed.

Various sectors of Indian Economy

There are 3 major sectors of Indian economy i.e. agriculture, industry and services **Agriculture :**

The share of agriculture in GDP was 55% in 1950-51, 52% in 1960-61 and came down to around 17% in 2009-10. Still dependent on monsoon rain. Agriculture provides raw material to various industrial activities. Agriculture sector provides employment to around 52% of India's work force.

Issues in agriculture: India was dependant for food on other counties till **1960. Green** revolution eliminated our dependence on other countries as India became **self-dependent in agriculture** production.

Indian agriculture is dependent on monsoon. There is low level of public investment. Yield of crop is low. There

is need for **2nd** green revolution. **Steps to** be undertaken, include: Growth of irrigated area

Reclamation of degraded land. Improvement in water management, rain water harvesting. Extension services to reduce the knowledge gap. Diversification into high value output such as fruits, vegetable, flowers, herbs etc. Provision for adequate credit.

Industry: It accounts for about 19% share in GDP.

Central Statistical Organisation (CSO) classifies the industrial sector into 3 segments (1) Mining and **quarrying (2) Manufacturing (3) Electricity, Gas and Water Supply:** Micro, Small and Medium Enterprises (MSME) sector is an important segment of industry.

Issues in industry: Indian industry was working in a closed environment till 1990s. After initiation of economic reforms, it was opened for foreign investment which resulted **into** flow of FDI. This helped in technology upgradation.

Micro and Small enterprises (MSEs) : It is an **important** segment of industrial sector. As per Annual Report of Ministry of SME 2006-07, this sector contributed 39% of industrial production, 34% of industrial exports and 35% of total **employment.** Annual growth rate of value of output was 16.8%, of exports 20% and of employment **4.4%.**

Problems faced by MSE include difficulty in **getting bank finance, insistence on collateral securityAigh interest rates, lack of supportingtusiness environment** etc.

Steps taken to help MSE sector : Fixing of mandatory sub-limits for loans to **MSEs** by **banks.**

Relaxation of collateral security for loans up **to Rs.to lac** and provision for guarantee cover from Credit Guarantee Fund Trust for MSE up to loan of Rs.100 lac as a substitute for collateral security. Enactment of MSME Development Act 2006Enactment of Interest on Delayed Payment Act 1998

Services: It account for about **64%** of GDP, This sector has gained at the expense of agriculture and industrial sector through the 1990s. The major components of this sector are Information Technology Enabled Services (IETS), Banking and Insurance, Construction and real estate, transportation and aviation etc. Issues in services sector : When services sector bypasses the industrial sector, economic growth can get distorted. Hence this sector must be°supported by proportion growth of industrial sector; otherwise growth may not remain sustainable.

Structural changes in Growth rates in various sectors of Indian Economy (in %age)

	1900-50	1951-80	1980s	1990s	2000-09
Agriculture	**Not available**	**2.1**	**4.4**	**3.2**	**2.8**
Industry	**Not available**	**5.4**	**6.4**	**5.7**	**6.5**
I	**Not available**	**4.5**	6.3	7.1	9.0
Total **GDP** I **Services**	**0.7%**	**3.5**	**5.6**	**5.7**	**7.2**

Structural changes in share in GDP for various sectors of Indian Economy (in %age)

	1950-51	1961-70	1970-71	1980-81	1990-91	2008-09
Agriculture	55	51	44	38	31	17
,industry	11	13	15	17	20	19
Services	34	36	**41**	45	49	64
Total GDP e	100	I 100	100	100	100	100

Indian Economy: A Brief Overview:

1. In the first five decades of the twentieth century, the per capita GDP in India was stagnant at 0.9 per cent with population growing by about 0.8 per cent.
2. The annual growth, averaged at around 3.5 per cent during the period 1950 to 1980.
3. The average growth rate of the Indian economy over a period of 25 years since 1980-81 was about 6.0 per cent.
4. The GDP growth rate has further accelerated averaging 7.2 per cent during the seven-year period 2000-01 to 2007-08, with the growth rate in the last five years (2003-04 to 2007-08) averaging 8.8

per cent.

5. Over the years, while the GDP growth has been accelerating, the population growth rate has moderated, giving a sharp impetus to the growth in per capita income.
6. The strengthening of economic activity in the recent years has been supported by a sustained increase in the gross domestic investment rates from 22.8 per cent of GDP in 2001-02 to 35.9 per cent in 2006-07. Over 95 per cent of the investment during this period was financed by domestic savings.
7. Since independence, the inflation rate, in terms of the wholesale price index (WPI), on average basis, was above 15 per cent in only five out of fifty years and was in single-digit for thirty-six of these years. On most - occasions, high inflation was due to food or oil shortages.
8. The inflation rate accelerated steadily from an annual average of 1.7 per cent during the 1950s to 6.4 per cent during the 1960s and further to 9.0 per cent in the 1970s before easing marginally to 8.0 per cent in the 1980s. The inflation rate declined from an average of 11.0 per cent during 1990-95 to 5.3 per cent during the second-half of 1990s.
9. In the last quarter century, the country has developed resilience to shocks. During this period, balance of payments crisis was witnessed only once, triggered largely by the Gulf war in the early 1990s. The Indian economy, in the later years, could successfully avoid any adverse contagion impact of shocks from the East Asian Crisis, the Russian crisis during 1997-98, sanction-like-situation in post-Pokhran scenario, the border conflict during May-June 1999 and Sub-prime Crisis.
10. Despite the recent encouraging performance, the Indian economy faces several severe challenges. These relate, in particular, to poverty, education, health, environment, physical infrastructure, and fiscal issues.

Various Sectors of the Economy

Agriculture

1. Agriculture is one of the most important sectors of Indian economy.
2. Agriculture (including allied activities) accounted for 17 per cent of the Gross Domestic Product (GDP-at constant prices) in 2008-09 as compared to 21.7 per cent in 2003-04.
3. Though, the share of agriculture in GDP has been declining over the years, its role remains critical as it accounts for about 52% of the employment in the country. The prosperity of the rural economy is also closely linked to agriculture and allied activities.
4. From a nation dependent on food imports to feed its population, today India is not only self-sufficient in grain production but also has substantial food reserves.
5. Green Revolution involved bringing additional area under cultivation, extension of irrigation facilities, the use of improved high-yielding variety of seeds, better techniques evolved through agricultural research, water management and plant protection through judicious use of fertilizers, pesticides and cropping practices. All these measures resulted in quantum increase in the production of wheat and rice.
6. Issues regarding Indian agriculture: Indian agriculture is heavily dependent on monsoons. The monsoons play a critical role in determining whether the harvest will be rich, average, or poor. The structural weaknesses of the agriculture sector are reflected in the low level of public investment, exhaustion of the yield potential of new high yielding varieties of wheat and rice, unbalanced fertilizer use, low seeds replacement rate, an inadequate incentive system and post-harvest value addition.

There is an urgent need for second green revolution in Indian agriculture. Following steps need to be taken to achieve this objective.

- Doubling the rate of growth of irrigated area;
- Reclaiming degraded land and focusing on soil quality;
- Improving water management, rain water harvesting and watershed development;
- Bridging the knowledge gap through effective extension services;
- Diversifying into high value outputs, fruits, vegetables, flowers, herbs and spices, medicinal plants, bamboo, bio-diesel, but with adequate measures to ensure food security;
- Providing easy access to credit at affordable rates.

Industry:

1. Industry accounts for 19 per cent of the GDP in 2008-09. About one-third of the industrial labour force is engaged in simple household manufacturing only. The different industry sectors of India witnessed

tremendous growth over the last 20 years. This growth is attributed to the Government of India's liberal economic policy with increased FDI.

2. Central Statistical Organization (CSO) classifies the industrial sector into 3 segments: Mining and Quarrying, Manufacturing and Electricity, Gas and Water Supply.

Micro and Small Enterprises (MSEs):

1. As per the data on micro and small enterprises (MSEs) in the Annual Report of Ministry of Micro, Small and Medium Enterprises, 2006-07, the sector accounted for around 39 per cent of total industrial production, 34 per cent of the exports in the industrial sector and around 35 per cent of total employment among units engaged in manufacturing and services.
2. The sector registered a robust annual average growth in value of output, exports and employment at 16.8 per cent, 20.0 per cent and **4.4** per cent, respectively during the expansionary phase of 2003-07, before showing signs of slowing down in 2007-08 particularly in respect of employment growth to 2.9 per cent.
3. Problems of MSE: The problems cited by MSE borrowers in obtaining access to bank finance are insistence on collaterals, Guarantees, limited outreach of banks, rigid approaches, high interest and other costs, complex documentation, lack of supporting business development services and so on.
4. From the banker's point of view, the critical factors affecting credit delivery to this sector are low equity base, absence of marketing tie up, diversion of funds, poor management and book keeping, higher NPAs, mounting of receivables due to delay in payment of bills especially during downturn.
5. Measures to increase flow of credit leading to almost three fold increase in the credit to this sector from public sector banks from Rs.67,600 crore as on March 31,2005 to Rs.1,90,958 crore as on March 31, 2009.
6. The major policies in regard to credit delivery to this sector are as follows.

- Inclusion of MSE (as per revised definition) in priority with sub limits for the micro units.
- Stipulation that collateral should not be taken for loans up to Rs.10 lakh to MSE units.
- Providing credit guarantee for collateral free loans from the Credit Guarantee Trust Fund administered by S1DBI.

Micro, Small And Medium Enterprises Development (MSMED) Act, 2006

- The MSMED Act, 2006 classifies enterprises broadly into two categories, viz., (i) manufacturing enterprises; and (ii) service enterprises. These broad categories are further classified into micro enterprises, small enterprises and medium enterprise, depending upon the level of investment in plant and machinery and equipment as the case may be.
- The existing provisions of the Interest on Delayed Payment Act, 1998 to small scale and ancillary industrial undertakings have been strengthened under the MSMED Act.
- The Act also provides for constitution of a National Board for Micro, Small and Medium Enterprises under the chairmanship of the Union Minister for MSME, with wide representation of stakeholders.

Services:

1. The Service Sector now accounts for about two third of India's GDP: 64 per cent in 2008-09.
2. The rise in the service sector's share in GDP marks a structural shift in the Indian economy and takes it closer to the fundamentals of a developed economy (in the developed economies, the industrial and service sectors contribute a major share in GDP while agriculture for a relatively lower share).
3. However, service sector growth must be supported by proportionate growth of the industrial sector; otherwise the service sector grown will not be sustainable. In India, phenomenal growth has been noticed in selected segments like IT/ITES, telecom, banking, insurance and real estate, and civil aviation.

Economic Survey – 2014-15: Highlights

Fiscal Deficit

1. India must meet its medium-term fiscal deficit target of 3 percent of GDP
2. Government will adhere to fiscal deficit target of 4.1 percent of GDP in 2014/15
3. Government should ensure expenditure control to reduce fiscal deficit
4. Expenditure control and expenditure switching to investment key Fiscal Consolidation

1. Govt remains committed to fiscal consolidation; to enhance revenue generation

2. India can balance short-term imperative of boosting public investment to revitalize growth with fiscal discipline
3. Outlook for external financing is correspondingly favourable

Growth

1. GDP growth at market prices seen between 8.1 - 8.5 percent in 2015/16 on new GDP calculation formula
2. Double digit economic growth trajectory now a possibility; 8–10 per cent GDP in coming years
3. Total stalled projects seen at about 7 percent of GDP, mostly in private sector

Inflation

1. Inflation shows declining trend in 2014/15
2. Consumer inflation in 2015-16 to be between 5-5.5%; likely to be below central bank target by 0.5 - 1 percentage point
3. Lower inflation opens up space for more monetary policy easing
4. Government and central bank need to conclude monetary framework pact to consolidate gains in inflation control

Current Account Deficit

1. External Sector returning to strength, resilience
2. Estimated at about 1.3 percent of GDP in 2014/15 and less than 1.0 percent of GDP in 2015/16

Subsidies: Overhauling of subsidy regime would pave the way for expenditure rationalisation

Liquidity: Liquidity conditions expected to remain comfortable in 2015/16

Reforms

1. There is scope for big bang reforms now
2. India can increase public investments and still hit its borrowing targets
3. More reforms on anvil; Goods and Services Tax, expanding direct benefit transfers to be game-changers

Others

1. Foodgrains production for 2014-15 estimated at 257.07 million tonnes; will exceed last 5-year average by 8.5 million tonnes
2. NITI Aayog, 14th Finance Commission to enhance fiscal federalism
3. Need balance between 'Make in India' and 'Skilling India'
4. Services sector negotiations at WTO crucial for India in removing many market access barriers
5. Revitalise PPP model to revive investment
6. Manufacturing and services equally important for growth
7. Labour, capital, land, market reform and skills to be engines of growth
8. JAM Trinity — Jan Dhan Yojana, Aadhaar, Mobile — to help transfer of funds to poor without leakage Shield domestic industry to promote 'Make In India'
9. Borrowings to fund investment, not for meeting expenses
10. Food subsidy bill in April-Jan up 20% to Rs. 1.08 lakh cr
11. Reform Railway's structure, commercial practices, overhaul of technology
12. Public investment key growth engine in short-run for Railways, but not a substitute for private investment
13. More disinvestments on the anvil in current fiscal
14. Under-recoveries on petroleum products to come down to Rs. 74,664 crore in 2014-15, from Rs. 1.39 lakh crore in FY14
15. 4Ds — Deregulation, Differentiation, Diversification, Disinter (better bankruptcy laws) — to push financial sector growth
16. Implementation of GST to boost GDP, exports
17. Suggests medium to long term fiscal policy to target deficit, expenditure
18. Global commodity prices to remain weak in 2015
19. Ecommerce sector to witness 50% growth in 5 years

ECONOMIC REFORMS

TRANSFORMATION:

1. The share of services in the national income has steadily increased with corresponding fall in the

contributions of agriculture and industry over the years. Services sector now accounts for nearly two third of total output as against less than half in the early 1980s and the 1990s. Share of industry declined marginally to 19 per cent from 20 per cent whereas share of agriculture registered a steep decline from 38 per cent to just 17 per cent.

2. Domestic economy has become far more integrated with rest of the world which is visible not only in terms of growing trade volumes; financial flows from and to the outside world have also been steadily growing.
3. India's economic transformation mainly started initiated in the early nineties when policies were liberalized.
4. .Reforms were initiated on account of twin economic imbalances, i.e. fiscal crisis and external payment crisis, as well international and domestic political events. These include¯collapse of erstwhile USSR and the East European socialist regimes and their march towards market oriented economic system and the spectacular success of 'socialist market economy' of China with the aggressive opening up since 1978 and its associated success in poverty reduction.
5. The reform process is being continued due to growing and widespread acceptance of the need for rapid economic growth that can be achieved by the market-oriented reforms. Besides, competing claims of various states on benefits of economic reforms has also helped in sustaining the momentum of reform process in India.

Economic Transformation — Real Sector

1. Real sector Policy measures mainly focused on the manufacturing sector in the early stages of reform process. Deregulation of industry by way of eliminating licensing¯requirement, overhauling of public enterprises, enhanced role for private sector, abolition of MRTP Act, automatic approval route for foreign investment, elimination of quantitative import restrictions and reduction in tariff rates created a conducive environment to gear up the industry to face growing domestic as well as external competition to which it was exposed by the reform process.
2. De-reservation of large number of items that were earlier meant to be produced exclusively in the small scale sector.
3. Liberalisation of foreign direct investment both in terms of scope and proportion of foreign ownership and with regard to procedural details.
4. Industry responded to reforms by undertaking massive restructuring of its operations by upgrading their technologies, expanding to more efficient scales of production, resorting to mergers and acquisitions both within and outside the country and refocusing their activities to the core-competence.
5. Entry of private sector and foreign direct investment that introduced competition and state of the art technology brought a sea change in the services sector.
6. Synergies provided by the manufacturing sector, liberalization of financial sector with entry of private sector and policy initiatives with regard to information technology led to surge in growth of services sector.
7. The boom in information technology (IT) and Information Technology and Enabled Services (ITES) sector led to an era of 'services-led growth' as India emerged as global hub for BPO/KPO services in the world.
8. India has advantages of the low wage structure, flexibility due to time zone differences and access to a larger and better talent pool provide globally active companies.
9. As transformation of industrial as well as services sector has overwhelmingly been based on capital intensive techniques requiring skilled manpower, relative shift in sectoral incomes has not resulted in commensurate relocation of surplus labour and more than three-fifth of population continued to draw its livelihood from the primary sector.
10. Though agriculture sector seems to have remained isolated from economic reforms, yet several steps relating to free movement of agricultural commodities, APMC Act permitting farmers to bypass the mandatory requirement of safe in regulated markets and relaxation of restriction under Essential Commodity Act, 1955 along with introduction of future trading brought major change in the pricing mechanism. National commodity" futures markets discover price rather manipulation by local traders. Banks in association with professionally managed godowns extend credit to farmers against warehouse receipts. Large consumer goods companieS directly source agricultural produce from the farmers. These developments have worked towards improving the terms of trade (TOT) for the agriculture

sector. Further, due to lowering of protection and rising disposable incomes, the consumption basket has changed significantly. Growing demand for milk, poultry products and horticulture products, has induced substantial diversification towards allied activities which now account for nearly three-fifth of total primary sector output.

Economic Transformation — Financial Sector:

1. Financial sector reforms have been carried out as per recommendations of (a) Narasimham committee report on financial sector reforms (1992) (b) Narasimham committee report on banking sector reforms (1998) and (c) S.H. Khan report of the working group for harmonizing the role and operations of Development Financial Institutions and banks. Reforms in financial sector complemented the real sector developments.
2. Financial sector reforms included deregulation of interest rates on loans and advances. Along with free pricing, removal of constraints in terms of participation, type of instruments, market infrastructure and policy environment helped a lot. However, there was a conscious decision to go slow on derivative products, a stand amply vindicated by the current global crisis and relative immunity of India's financial sector.

Money Market Reforms:

1. Reforms in money market were essentially aimed at providing avenues for the market players to deploy or access to short-term funds and a platform to the monetary authority to modulate liquidity in the system.
2. These reforms included freeing of interest rates on call and other money market instruments, introduction of Commercial Paper and Certificate of Deposit, exemption of inter-bank lending from reserve requirement, introduction of screen-based trading and rupee derivatives such as Interest Rate Swaps (IRS) and Forward Rate Agreements (FRA), enlarging the scope of Repo market by expanding the repo-able securities and eligible participants in the repo market and introduction of tripartite repo, i.e. Collateralized Borrowing and Lending obligation CBLO to create pure inter-bank call money market.
3. Call Money market was made a pure inter-bank market which resulted in reduced turnover in Call-Money market which shifted to repo and CBLO market and daily average volumes in call market got almost half in 2008-09 from Rs.23,161 crore in 1999-2000. Volumes in case of market repo, on the other hand, rose by two-fold during the period and in case of CBLO increase has been four-fold during 2004-05 to 2008-09. Besides, reforms also lent stability to the market as volatility in call market got reduced by nearly half in the current decade from levels prevailing in the 1990s.

Government Securities Market:

1. The system of borrowing by Government at sub-market rates by increasing SLR was abolished and market auction system was introduced.
2. Automatic monetization was replaced with Ways and Means Advances (WMA).
3. The annual turnover in the market has grown from about Rs.2.8 lakh crore in 1998-99 to Rs.56.3 lakh crore in 2007-08. Yields on G-Sec now provide benchmark for pricing of securities in other markets.
4. With reforms, G-Sec is no longer a captive market. Investment in G-Sec by the banks is based on their commercial judgment rather than being dictated by the reserve requirement.

Foreign Exchange Market:

1. Prior to reforms, foreign exchange market was virtually absent. Exchange- earners were required to surrender/purchase foreign exchange from Reserve Bank at the reference rate. In this highly regulated system, very few transactions used to take place among the authorized dealers and trades were required to be squared off by the close of the day.
2. Reforms included introduction of market-based exchange rate regime, adoption of current account convertibility and relaxation on capital account, inter alia, in terms of permission to run open positions, to hold investments abroad and to retain foreign exchange along with introduction of hedging tools (derivatives) which led to emergence of active and vibrant foreign exchange market.
3. Exchange rate is now flexible and market determined; and capital account is also effectively convertible for the non residents. With significant liberalization on the capital account and given that market forces play a predominant role in determining external value of the rupee, there has not been large volatility in this market.

Capital Market:

1. Primary market witnessed a significant movement away from Controller of Capital Issues (CCI) regime imposing primary issuance at sub-market rates to free pricing and book-building system along with mandatory disclosures as prescribed by SEBI.

In the secondary market, corporatization of exchanges, screen-based trading replacing open outcry system, introduction of options and futures replacing erstwhile Badla System, rolling settlement replacing 14 day settlement cycle, dematting of securities with depository system created state-of-the-art infrastructure comparable to best international security. **Credit Market:**

1. Prior to reforms, interest rates were regulated both on deposits and advances and there was no incentive to cut cost, raise efficiency or upgrade credit assessment skills.
2. Reforms has resulted in more competition along with higher flexibility and operational autonomy to the banks. Further, stability of the banks is being ensured by emphasizing building up of risk management capabilities and introduction of prudential regulation and supervision in line with best international practices.
3. Widening of ownership due to stock market listing and associated disclosure requirements brought greater market discipline and transparency in the bank management.
4. There has been steady decline in intermediation cost of banks from 6.24 per cent in 1991-92 to 3.43 per cent in 2006-07.
5. Growth has been higher for urban and semi-urban branches compared to rural branches. In terms of advances to various sectors of the economy banks' portfolio has been quite diversified.

Payment Systems:

1. Payment and Settlement Systems Act, 2007 was enacted empowering the Reserve Bank of regulate and supervise payment and settlement systems, lay down policies and providing a legal basis for multilateral netting and settlement finality.
2. Use of other bank ATMs has been made free of cost for saving bank customers with effect from 1 April 2009 subject to maximum 5 withdrawals per month and max withdrawal per transaction restricted to Rs 10000.
3. The service charges for 'Electronic Payment Products' and outstation cheques have been rationaised. Speed clearing has been introduced to reduce time taken for collection of outstation cheques.
4. 'Cheque Truncation System (CTS)' has been introduced in cheque clearing since July 2008 in New Delhi.
5. More than 60,000 branches of banks are participating in National Electronic Funds Transfer (NEFT) system.

Economic Transformation - integration with the Global Economy:

1. In India, the share of merchandise exports to GDP increased from 5.8 per cent in 1990-91 to 15.1 per cent in 2008-09, the share of merchandise imports as percentage to GDP, on the other hand, increased from 8.8 per cent to 25.5 percent during the same period.
2. On the import side, India's demand for primary products, viz., raw materials and energy has increased since 1990s, which may be linked to its rapid economic growth. **In** 2007, India was the 7^{1}" largest oil importer of the world.
3. While, India's merchandize trade_has grown many folds in the current decade, during 2008, India ranks 26th in the world with a share of 1.1 per cent.
4. However, in terms of commercial services exports, India ranks much higher at 9th in the world with a share of 2.7 per cent.
5. Net capital inflows increased from US $ 7.1 billion in 1990-91 to $ 45.2 billion in 2006-07, and further to $ 108.0 billion during 2007-08. The gross volume of capital inflows, however, amounted to $428.7 billion in 207-08 as against an outflow of $320.7 billion.
6. Apart from a swift transition to a market determined exchange rate regime, other important reforms measures included dismantling trade restrictions, moving towards current account convertibility, liberal inflows of private capital, removal of restrictions on all inflows and related outflows, as also, gradual liberalisation of certain restrictions on outflows.

Trade Liberalization: De-licensing of virtually all intermediate inputs and capital goods, progressive

reduction in tariff rates along with permission for all current business transactions, expenses for education and medical and foreign travel enabled India to accept IMF Article VIII obligation thereby making rupee convertible on current account as early as in 1994. Further liberalization with regard to import licensing for consumer goods and reduction of tariff rate below 10 per cent (barring few exceptions, such as automobiles) considerably enhanced the outward orientation of Indian economy.

Capital Account: The move towards full capital account liberalization has been calibrated with extreme caution. There has been preference for non debt capital compared to debt capital.

Foreign Direct Investment:

1. The major policy, thrust towards attracting foreign direct investment (FDI) began in the early 1990s by introduction of automatic approval route that empowered RBI to approve equity investment up to 51 per cent in select 34 priority industries.
2. Currently, unless there is specific restriction contained in FDI policy, 100 per cent foreign investment is permitted under automatic route.
3. A very limited number of activities fall under this category, viz., retail trading, atomic energy, lottery business, gambling an betting.
4. The list for FDI cap below 100 per cent is also quite short including broadcasting, print media, defence, insurance, asset reconstruction, investment companies, petroleum and air transport.

Portfolio Investment:

1. Portfolio investment both in primary and secondary market by Foreign Institutional Investor (FII) was opened up in 1992. At the same time, Indian companies were permitted to raise equity finance through issue of GDR and ADR in Europe and American markets.
2. Policy with regard to Fll investment was progressively liberalized with total Fll share in equity being raised from 24 per cent to total sectoral cap on foreign investment. For majority of sectors this cap is 100 per cent.
3. Besides, HI are permitted to invest in debt instruments issued by both private corporate and the Government, and they can operate in forward market to hedge their currency risks.

External Commercial Borrowings (ECB):

1. Net inflow on account of ECB rising from USD 5 billion in 2004-05 to more than USD 22 billion in 2007-08.
2. The policies towards ECB that include bank loans, buyers' credit, suppliers' credit have been decided by the overall consideration of prudent external debt management by keeping the maturities long, cost low and priority for projects in the infrastructure and core sectors.

Outward Flows:

Outward capital flows have also been relaxed for both individuals and the corporate sector. Firms can invest abroad up to their net worth plus EEFC holdings and also the foreign exchange raised through ADR/GDR.

Impact of Reforms:

1. Improvement **in** terms of efficiency, competitiveness and productivity.
2. Higher economic growth with far greater integration with the rest of the world in terms of diversification of good and services as well as destinations to which exports are being made.

ISSUES IN REFORMS

There are various issues like how far the benefits of economic progress have percolated down? Whether standard of living of the population has uniformly improved? Can we say economic transformation has brought prosperity to public at large and could we make dent in poverty?

Poverty:

1. **There** has been improvement regarding poverty measured on the basis of consumption expenditure, both in rural and urban areas. There is about 7 to 8 percentage points decline in poverty ratio in 2004-05 over 1993-94 and improvement being more predominant in the rural areas.
2. Divergence **in** income distribution has worsened further sine the early nineties. Gini Coefficient, a standard measure of income/expenditure inequality, has further deteriorated from 32.9 per cent in 1993 to 36.2 per cent in 2004.
3. As per NSS 61st round, per capita consumption expenditure of more than 60 per cent population was less than Rs.20 per day in 2004-05.

Socio-Economic Development:

1. Human Development Index **(HDI),** a widely indicator of socio-economic conditions has placed India at 132 out of 179 countries in the world in the year 2006 - deterioration from a relatively better ranking of 121 in the year 1990.
2. This implies countries in the world have grown and improved their lot much faster than India. This slip in ranking is broadly reflective of poor performance in terms of health and education services.

Health:

1. **There** has been significant improvement over the years in terms of various demographic indicators such as life expectancy, infant and child mortality and maternal mortality rates. However, in terms of international comparison, India slipped further in terms of ranking and continues to lag behind otherwise comparable countries in the world.
2. Per capita expenditure on health services in India in 2006 has been lowest among select countries-just half of that spent by Sri Lanka and a bit lower than that spent by Nigeria.
3. Poor infrastructure is reflective of a small share of GDP devoted to health services and efforts need to be made in terms of public-private partnership.

Education:

1. 86th constitutional amendment has made free and compulsory education to all children of 6 to 14 years of age a fundamental right. Right to Education Act was passed in 2010.
2. Overall there is improvement as discernible from gross enrolment ratio. However, in 2006, 8.9 per cent of children of age 6-14 years in rural areas still remain out of school.
3. In terms of public spending on education, there has been some marginal improvement from 3.6 per cent of GDP *in* 1993 to 4.01 per cent of GDP in 2002.
4. As per one estimate made in 2006, overall teacher absenteeism has been at 25 per cent in India, compared with 16 per cent in Bangladesh and 29 per cent in Uganda.
5. Quality of education is another area of major concern. In a survey, less than 9% of student in 'I^{s}' and 2nd grade could read their respective text books. Nearly half of the 5th grade students are unable to read level 2 texts.

Way Forward

Agricultural Investment:

1. The share of agriculture in total income has dropped to 17 per cent; still more than 60 per cent of population continues to draw its livelihood from this sector. This workforce also accounts for sizeable proportion of poor **in** the country.
2. There is an urgent need to enhance investment in agriculture sector not only to raise crop productivity, but also to create employment opportunities outside the farming.
3. There is a need to effectively integrate rural sector with urban economy by creating needed infrastructure, viz., roads in rural areas; electricity; major and minor irrigation projects and cold-storage chains to provide farm producers access to urban markets.
4. Besides, there is also a requirement felt for bringing legal reforms with regard to tenancy rights that would give a boost to contract farming and higher productivity in farming activity particularly when individual arm size is rapidly dwindling.

Labour Reforms:

1. The labour laws should help in bringing market efficiency and productivity and oriented towards encouraging and promoting the growth of the entrepreneurs, creating a positive investment environment and opportunities.
2. There is a need to ensure relativity in the rights of management and workers to promote healthy milieu for growth and progress.
3. A liberal exit policy can only coexist with generous unemployment benefits, retraining benefits and severance pay.
4. The disparity between the organized and the sectors in terms of working condition and protection of employees' rights also needs to be bridged.
5. There is a need to enhance protection of workers in the unorganized sector with provision of

insurance, pension schemes, medical facility and vocational training.

Demographic Dividend:

1. Share of the working age group (15-64) **in** the population has been increasing since the 1980s and has been projected to be in the range of 62 to 68 per cent during first quarter of current century.
2. However, for these demographic changes to provide upward push to economic growth, it needs to be accompanied by process of skill formation and employment opportunities. This would require larger investment in human capital formation and encouragement to entrepreneurial activities by creating conducing environment.

Financial Inclusion:

1. It is felt that benefits of growth have not percolated down to the underprivileged sections. Financial Inclusion initiatives, are constrained by several factors.
2. High operating cost in remote areas, small ticket size, lack of collaterals and illiteracy have obstructed the steps towards financial inclusion.
3. Availability of banking technology shows that poor are bankable with good business prospects. Technology should be used to make the transaction cost cheaper and affordable for the poor.

Economic Policy, Monetary Policy and Fiscal Policy

ECONOMIC POLICY

Economic policy refers to the positive and negative actions that the government of a country generally initiates, in the economic field. The policy has a direct bearing on the economic strength and its ranking of a country in the world economy in economic numbers.

The policy sets the economic priorities of the govt., (a) national ownership of resources (b) the level of government income and spending (c) money supply and interest rates (d) conditions in the labour market and (e) many other areas of government interventions.

Economic policies are often influenced by the social and political environment within the country. It is also affected by the degree of integration of the economy with other economies of the world and the international : institutions like the International Monetary Fund or World Bank.

Objectives of economic policy

1. **Full employment -** This ensures creation of opportunities where there are jobs for all of those, who are willing to work (it needs to be noted that full employment does not mean employment for all).
2. **Inflation control -** This keep the purchasing power of the currency stable and real wage high. Increasing prices reduce the purchasing power of the currency and indirectly affect the standard of living.
3. **GDP growth -** This is major objective of the economic policy, as it increases the income of the people. If there is increase in per capita income of the population, it leads to better standrd of life, provided there is equitable distribution of income.

Other policies that support the economic policy

The following policies provide support for achieving the economic policy goals:

1. **Fiscal policy - It** is the income, expenditure and tax policy of the govt. This policy is generally executed through annual budget exercise. Through this policy the govt. is able to impact almost all sectors of the economy. The policy determines the tax rates and duties to be charged or tax concessions to be given. In addition, the policy decides the area in which investments are to be made or disinvestments to be made etc.
2. **Monetary policy -** It is concerned with the amount of money in circulation and consequently, the interest rates and inflation. The policy ensures availability of adequate liquidity for growth of the economy. It also ensures that there should not be excessive liquidity as that results in inflation. Monetary stabilization stimulates an economy out of recession and the constrained money supply prevents the excessive inflation.

Credit policy - This policy ensures that all the productive sectors of the economy get adequate credit at reasonable interest rates. This policy is announced by the Central Bank of the country (RBI in India). Through the policy, the Reserve Bank impacts the flow of credit to various sectors, the cost of deposit and cost of credit etc.

4. **Trade policy :** This policy relates to internal and external trade of the country. The issues relating to tariffs, trade agreements and the international institutions are also dealt with through this policy. **The other policies** which help the economic policy are agriculture policy, industrial policy, HRD policy, redistribution policy etc.

MONETARY POLICY

Monetary policy consists of measures aimed at altering the economy's money supply and in turn the interest rates, for stabilizing the aggregate output, employment and price level. In effect, monetary policy is a tool to regulate the interest rate and money supply expansion that prevail in the economy. RBI is vested with the powers for formulating, supervising and controlling the monetary and banking system.

Instruments: There are 2 instrument of monetary policy.

(1) Under the general category, it has powers to conduct **open market operations (OMO), change the reserve ratios** and **alter the discount rates.**

(2) Under special category it can have various credit direction program (priority sector, export credit, food credit etc.) and specifying margins and level of credit in special categories (selective credit control). **Easy or tight money :**

(1) An easy money policy is intended to increase the money supply in the economy and as a result bring about a reduction in interest rates. Lower interest rates are expected to stimulate a sluggish economy. RBI buys securities from banks or reduce the reserve ratio or the bank rate. RBI usually follows an **easy policy** in times of recessions and economic slowdown.

(2) Tight policy is intended to cool down an overheated economy by limiting credit availability or making it exorbitantly costly. For this, RBI employs measures which would reduce the overall money supply, which basically are the reverse of what is adopted for an easy money policy. A **tight money policy** is implemented when economy suffers from inflationary pressures.

Open market operations : It refers to buying and selling of govt. securities by RBI in the open market. By its impact on the reserves of banks, OMO helps control the money supply in the economy. When RBI sells Govt. securities to banks, the lendable resources of the banks are reduced and banks are forced to reduce or contain their lending, thus curbing the money supply. When money supply Is reduced, the consequent increase in the interest rates tends to limit spending and investment.

Varying Resent l Ratios: An increase in CRR or SLR would force banks to appropriate a larger part of their lendable resources as reserves. As banks reduce their market lending operations, the consequent decline in, money supply would increase interest rate.

Bank rate / Repo Rate : When these rates are increased, banks reduce their borrowing from **RBI,** which lowers their lendable resources. The decline in money supply increases the interest rates. The opposite happens when RBI reduces these rates.

Of three kinds of general monetary instruments, OMO is found to be more flexible and preferred.

MONETARY & LIQUIDITY MEASURES & AGGREGATES

The current measures, monetary (M) and liquidity (L) aggregates were implemented in June 1998 as per YB Reddy Committee recommendations.

MONETARY AGGREGATES

M 0 **(weekly report)**	Currency in circulation bankers' deposits with RBI other deposits with RBI (including primary dealers' balance)
M 1 **(called Narrow money)** **fortnightly report**	currency with public current deposits with banking system 15% of demand liabilities portion of saving deposits with banking system Other deposits with RBI.
M 2 **fortnightly report**	M1+ time liabilities portion (i.e. remaining 85%) of saving deposits with banking system certificates of deposits Issued by banks term deposits (excluding FCNR-B deposits) with a contractual maturity of up to and including one year with banking system

M3 **(Called Broad money)** **fortnightly report**	M2+ term deposits (excluding FCNR-B) with a contractual maturity of over one year with the banking system ' call borrowings from non-depository financial corporations by the banking system.

LIQUIDITY AGGREGATES

LI	M3+ all deposits with post office saving banks (excluding NSCs)
L2	L 1+ term deposits with term lending institutions and refinancing institutions (Fls) term borrowing by Fls + certificate of deposits issued by Fls and
L3	• L 2+ • public deposits of NBFCs.

The analysis of the prescribed aggregates reflects that MO is essentially the monetary base, compiled from the balance sheet of RBI. M1 purely reflects the non-interest bearing monetary liabilities of banking system (from 1.4.10 some element of interest payment has come in due to payment of interest on saving bank on daily product basis). M 2 includes besides currency and current deposjts, saving and short term deposits reflecting the transactions balances of entities. M3 has been redefined to reflect additionally to M2, the call funding that the banking systems obtains from other financial institutions.

What is Monetary Policy?:

1. Monetary policy is the process by which the government, central bank or monetary authority of a country controls: (i) the supply of money, (ii) availability of money and (iii) cost of money or rate of interest, in order to attain a set of objectives oriented towards the growth and stability of the economy.
2. Monetary policy may be expansionary policy, or a contractionary policy.
3. An expansionary policy increases the total supply of money in the economy, and a contractionary policy decreases the total money supply.
4. Expansionary policy is traditionally used to combat unemployment in a recession by lowering interest rates, while contractionary policy involves raising interest rates in order to combat inflation.
5. Monetary policy is contrasted with fiscal policy, which refers to government borrowing, spending and taxation.

Tools of Monetary Policy:

Bank Rate:

1. Bank rate, also referred to as the discount rate, is the rate of interest which a central bank charges on he loans and advances that it extents to commercial banks and other financial intermediaries.
2. Changes in the bank rate are often used by central banks to control the money supply. However, the role of the bank rate as an instrument of monetary policy has been very limited in India because of these basic factors:

(a) The structure of interest rates was administered by RBI — they are not automatically linked to the bank rate;

(b) Commercial banks enjoy specific refinance facilities, and not necessarily rediscount their eligible securities with RBI at bank rate; and

(c) The bill market is under-developed and the different sub-markets of the money market are not influenced by the bank rate.

Cash-Reserve Ratio (CRR):

1. The present banking system is called a "fractional reserve banking system', as the banks are required to keep only a fraction of their deposit liabilities in the form of liquid cash with the central bank for ensuring safety and liquidity of deposits.

2. The Cash Reserve Ratio refers to this liquid cash that banks have to maintain with the Reserve Bank of India (RBI) as a certain percentage of their net demand and time liabilities.
3. CRR is an important and effective tool for directly regulating the lending capacity of banks and controlling the money supply in the economy. CRR is increased when money supply is increasing and causing an upward pressure on inflation.

Statutory Liquidity Ratio (SLR)

1. Statutory Liquidity Ratio refers to the amount that all banks require maintaining in cash or in the form of Gold or approved securities. Statutory Liquidity Ratio is determined as percentage of net demand and time liabilities.
2. In India, Reserve Bank-of India determines the percentage of Statutory Liquidity Ratio. At present (with effect from 18th Dec 2010), the minimum limit of Statutory Liquidity Ratio set by the RBI is 24 per cent.
3. The main objectives for maintaining the Statutory Liquidity Ratio are the following:

- Statutory Liquidity Ratio is maintained in order to control the expansion of Bank Credit. By changing the level of Statutory Liquidity Ratio, Reserve bank of India can increase or decrease bank credit expansion.
- Statutory Liquidity Ratio in a way ensures the solvency of commercial banks.
- By prescribing Statutory Liquidity Ratio, Reserve Bank of India, in a way, compels the commercial banks to invest in government securities like government bonds.

Market Stabilization Scheme (MSS):

1. MSS was introduced when due to heavy inflow of US dollars by FIIs and purchase thereof by RBI created enormous liquidity.
2. As a response to the large-scale capital inflows and the consequent problems faced in managing liquidity, the Reserve Bank introduced the Market Stabilization after consulting the Government of India for mopping up liquidity of a more enduring nature in March 2004.
3. Under this scheme, the government would issue existing instruments, such as, Treasury Bills and/or dated securities by way of auctions under the MSS, in addition to the normal borrowing requirements, for absorbing liquidity from the system.

4. The intention of MSS is essentially to differentiate the liquidity absorption of a more enduring nature by way of sterilization from the day-to-day normal liquidity management operations.

Repo:

1. Repo (Repurchase) rate is the rate at which the RBI lends shot-term money to the banks. When the repo rate increases borrowing from RBI becomes more expensive.

2. In case, RBI wants to make it more expensive for the banks to borrow money, it increases the repo rate; similarly, if it wants to make it cheaper for banks to borrow money, it reduces the repo rate. Bank lending rates are determined by the movement of Repo Rate.

Reverse Repo:

1. Rate at which banks park their short-term excess liquidity with the RBI. The RBI uses this tool when it
2. feels there is too much money floating in the banking system. An increase in the reverse repo rate means that the RBI will borrow money from the banks at a higher rate of interest. As a result, banks would prefer to keep their money with the RBI.
3. Repo Rate signifies the rate at which liquidity is injected in to the banking system by RBI, whereas reverse repo rate signifies the rate at which the central bank absorbs excess liquidity from the banks.

Open Market Operations (OMO)

1. Under the OMO, the RBI buys or sells government bonds in the secondary market. By absorbing bonds, it drives up bond yields and injects money into the market. When it sells bonds, it does so to suck money out of the system.

How did Monetary Policy in India respond to Global Financial Crisis?: (i) the repo rate was reduced by 425 basis points to 4.75 per cent, (ii) the reverse repo rate was reduced by 275 basis points to 3.25 per cent, (iii) the cash reserve ratio (CRR) was reduced by a 400 basis points to 5.0 per cent, and (iv) the actual/potential provision of primary liquidity was of the order of Rs.5.6 trillion (10.5 per cent of GDP).

RBI'S Monetary Policy Aims to achieve the Following Objectives:

- Monitor the 'global' and 'domestic' economic conditions and respond swiftly as required.
- Ensure higher bank credit expansion to achieve higher growth but at the same time protect the credit quality.
- Maintain price stability and financial stability.
- Give thrust on Interest Rate Management, Inflation management and Liquidity management.

FISCAL POLICY

The **fiscal policy** is the policy relating to government expenditure and revenue collection, to influence the economic activity. The two main instruments of fiscal policy are government expenditure and taxation. The change in the level and composition of taxation and government spending can impact the following variables :

1. Aggregate demand and the level of economic activity;
2. The pattern of resource allocation;
3. The distribution of income.

Stance of fiscal policy

The 3 possible stances of fiscal policy are neutral, expansionary and contractionary.

(a) A **neutral stance** of fiscal policy implies a balanced economy. This results in a large tax revenue. Government spending is fully funded by tax revenue and overall, the budget outcome has a neutral effect on the level of economic activity.

(b) An **expansionary stance** of fiscal policy involves government spending exceeding tax revenue.

(c) A **contractionary fiscal policy** occurs when government spending is lower than tax revenue.

Deficits

If the govt. spending is higher than the govt. revenue, there will be deficit, which can be a revene deficit, fiscal deficit or primary deficit.

(a) Revenue deficit = Revenue expenditure - revenue receipts.

(b) Fiscal deficit = Total expenditure - (revenue receipts + capital receipts other than borrowing).

(c) Primary deficit = Fiscal deficit - interest payments.

There are various methods of funding of these deficits. Fiscal deficit is generally financed by borrowing by the govt. by safe of treasury bills or by raising long term loans etc. This borrowing entails interest cost and in case it increase beyond the reasonable level, it can create default problem and resultant effects as happened in certain European countries during 2010.

Methods of funding

Govt spends money on a wide variety of things, from general administration to the military and police to services like education and healthcare, as well as transfer payments such as welfare benefits. This expenditure can be funded by way of Taxation, Seigniorage (by printing money), Borrowing money from the population or from abroad, Consumption of fiscal reserves, Sale of fixed assets (e:g., land) i.e. disinvestment. All of these except taxation are forms of deficit financing.

Economic effect of fiscal policy

Governments use fiscal policy to influence the level of aggregate demand in the economy, in an effort to achieve economic objectives of price stability, full employment, and economic growth. Increasing the govt spending and decreasing tax rates are the methods to stimulate aggregate demand. This can be used in times of recession or low economic activity as an essential tool for building the framework for strong economic growth and working towards full employment.

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FRBM ACT:

1. Introduced on the recommendations of a committee headed by Dr. E.A.S. Sharma.
2. Law was enacted in August 2003.

What the Act Requires

1. It requires the Government to place before Parliament three statements each year along with the Budget, covering Medium Term Fiscal Policy, Fiscal Policy Strategy and Macroeconomic Framework.

2. The Act lay down fiscal management principles, making it incumbent on the Centre to 'reduce the fiscal deficit' (no target is mentioned in the Act, but the Rules prescribe 3 per cent of GDP) and, more categorically, to 'eliminate revenue deficit' by 31 March 2008.
3. The Act requires the government to set a ceiling on guarantees (the Rules prescribe 0.5 per cent of GDP. The ceilings may be exceeded on grounds of "national security or national calamity **or** such other exceptional grounds as the Central Government may specify."
4. The Act prohibits the Centre from borrowing from the Reserve Bank of India-that is , it bans 'deficit financing' through money creation. The RBI is also barred from subscribing to primary issues of Central Government securities. Temporary Ways and Means advances to tide over cash flow problems are permitted. Exceptions are also allowed whenever the Government declares an exceptional situation.
5. The Finance Minister is required to keep Parliament informed through quarterly reviews on the implementation, and to take corrective measures if the reviews show deviations. The Act provides that no deviation shall be permissible 'without the approval of Parliament'
6. The main theme of FRBM Act is to reduce the dependence of the Government on borrowing and help to reduce the fiscal deficit in a phased manner.

MONETARY POLICY STATEMENT : 2015-16 THIRD BI-MONTHLY

The Reserve Bank of India has announced its Third BI-Monthly Monetary Policy Statement, 2015-16 on the very expected lines of maintaining the status quo with regards to the changes in the policy rates.
The RBI awaits resolution of uncertainty related to the persistence of recent inflationary pressures, the eventual monsoon outturn and the rate action by the US Federal Reserve; improved transmission of past cuts by Banks; and additional steps to unclog supply side bottlenecks by the Government.
The extent of progress on such factors in the coming two months would critically determine whether the Central Bank has adequate room to reduce the Repo rate in the ensuing policy review, at the end of September 2015.

KEY TARGETS:

CPI inflation projections for January-March 2016 lowered by 0.2% to 6.1%; risks broadly balanced around the forecast of 6.0% CPI inflation for January 2016. This marks a moderation from the June 2015 policy review, in which the RBI had viewed risks to its forecast of 6.0% inflation for January 2016, as tilted to the upside. Projection for output growth for 2015-16 maintained at 7.6%; gradual improvement seen in growth outlook.

MONETARY AND LIQUIDITY MEASURES:

On the basis of an assessment of the current and evolving macroeconomic situation, it has been decided to:

- **REPO RATE:** The policy Repo rate under the liquidity adjustment facility (LAF) unchanged 6.75%.
- **CASH RESERVE RATIO:** The Cash Reserve Ratio of scheduled banks has been retained at 4% of their net demand and time liabilities (NDTL);
- **STATUTORY LIQUIDITY RATIO (SLR):** The Statutory Liquidity Ratio of scheduled commercial banks remains unchanged at 21.5% of their NDTL.
- **REVERSE REPO RATE:** The Reverse repo rate determined with a spread of 100 basis points stands at 5.75 %.
- **MARGINAL STANDING FACILITY (MSF):** The MSF rate stands at 7.75%.
- **BANK RATE:** The Bank Rate remains at 7.75% The MSF rate and the Bank Rate are calibrated to 100 basis points above the repo rate.
- **TERM REPOS:** To continue to provide liquidity under overnight repos at 0.25% of bank-wise NDTL, & liquidity under 7-day & 14-day term repos of up to 0.75% of NDTL of banking system through auctions. Further, RBI has decided to continue with daily one-day term repos & reverse repos to smooth liquidity.

GLOBAL ENVIRONMENT:

- The global economic activity has recovered modestly. The US economy rebounded on stronger consumption growth and steadily improving labour market conditions.
- The Euro area has grown at a moderate pace through the first half of 2015, supported by consumer spending, easing financing conditions and a modest downturn in still-high unemployment.

- In Japan, growth slowed in Q2. Domestic consumption is still weak, but manufacturing activity picked up strengthening exports and corporate profitability which could stimulate capital spending.
- In the emerging market economies (EMEs), activity decelerated due to headwinds from weak external demand, tightening external financing conditions, deteriorating structural bottlenecks and spill overs from unsettled conditions in financial markets.
- Despite aggressive policy Chinese economy is slowing on macroeconomic rebalancing, sizable stock market corrections, a cooling property market and excess capacity in several mfg industries. Recessionary conditions persist in both Russia and Brazil, with downside risks from commodity prices and geopolitical developments casting a shadow on the outlook, including for other EMEs.
- In recent months, financial markets have experienced high turbulence due to the Greek crisis, the Chinese stock market slump and shifts between risk-on and risk-off sentiments based on changes in beliefs about when the Federal Reserve will start raising rates. Bond market sell-offs originating in Germany lifted bond yields across the world tightened financing conditions. Equity markets were buoyed by the search for yields which stretched asset valuations until end-June, when sharp stock market corrections in China pulled down share prices globally.

DOMESTIC ENVIRONMENT:

- In India, the economic recovery is still work in progress. The monsoon is near normal. Consequently, kharif sowing has expanded significantly relative to a year ago, especially in respect of oilseeds, pulses, rice and coarse cereals. If prospects of a good harvest strengthen, currently weak rural demand will improve to provide an important boost to activity.
- Shrinking exports in some industries, in part a result of weak global demand and global overcapacity in those industries and in part a result of the significant depreciation of currencies of some major trading partners against the rupee, also contributed to weak aggregate demand.
- Although overall business confidence is positive, the level of optimism was a shade lower in April-June than in the preceding quarter. Investment, as measured by new projects, is still weak, primarily because of still-low capacity utilization. In the critically important power sector, where final demand is strong, the recent step-up in generation in response to the commendable easing of bottlenecks in coal supply is being partly negated by structural problems relating to clogging of transmission grids and the dire financial state of electricity distribution companies.
- There are signs that consumption demand, especially in urban areas, is picking up. Car sales were strong. Nominal bank credit growth is lower than previous years, but adjusted for lower inflation as well as for lower borrowing by oil marketing companies and increased borrowing from commercial paper markets, credit availability seems to be adequate for most sectors.
- The services sector continues to emit mixed signals. The pick-up in heavy commercial vehicle sales and rising port and domestic air freight suggest strengthening transportation activity.
- Headline consumer price index (CPI) inflation rose for the second successive month in June 2015 to a nine-month high on the back of a broad based increase in upside pressures, belying consensus expectations. The sharp month-on-month increase in food and non-food items overwhelmed the sizable 'base effect' in that month. Food inflation rose 60 basis points over the preceding month, driven by a spike in prices of vegetables, protein items. Near-term inflation expectations of households returned to double digits after two quarters, although those of professional forecasters remained anchored.
- The Liquidity conditions have been very easy. A seasonal reduction in demand for currency and increased spending by Govt. coupled with structural factors such as low credit deployment relative to the volume of deposit mobilization contributed to surplus conditions in the money markets. This resulted in a significantly lower average daily net liquidity injection under the fixed rate repos under LAF, and variable rate term repo/reverse repo and MSF.

VARIOUS RATES AT GLANCE (As on 31.07.2015)		
Bank Rate	8.25%	02.06.2015
CRR	4.0%	09.02.2013
SLR	21.5%	07.02.2015
Repo Rate	7.25%	02.06.2015
Reverse Repo Rate	6.25%	02.06.2015
MSF Rate	8.25%	02.06.2015

VARIOUS RATES AT GLANCE (As on 31.10.2015)			
BANK RATE	7.75%	**Base Rate of major Banks**	9.30-9.70%
CRR	4.00%	**FOREX RESERVES- Rs. (Billion)**	22,826.9
SLR	21.5%	**FOREX RESERVES US $ Million**	353,069.0
REPO RATE	6.75%	**SCB Total Deposits - Rs. in Cr.**	91,638.2
Reverse REPO	5.75%	**SCB Total Credit - Rs. Cr.**	68,302.4
MSF	7.75%	**CREDIT- DEPOSIT RATIO**	74.53%

GDP CONCEPTS

Gross Domestic Product (GDP): It is the total market value of all the final goods and services produced within the territorial boundary of a country, using domestic resources, during a given period of time, usually one year. Gross National Income (GNU) at Market Prices = GDP at market prices + taxes less subsidies on production and imports (Net receivable from abroad) + Compensation of Employees (Net receivable from abroad) +property income (Net receivable from abroad)

Gross **National** Product (GNP) is equal to GDP (+) total capital gains from overseas investment (-) income earned by foreign national domestically

GNP = GDP + NR (Net income from assets abroad (Net Income Receipts)

GDP Computation

. According to the National Income Accounting, there are three ways to compute GDP:

1. Expenditure wise: Calculating the total expenditure of all the entities.
2. Income Wise : Calculating the total incomes received by factors of production — land, labour, capital and entrepreneur.
3. Product Wise : Calculating the total production.

Expenditure Method: As per this method, GDP = consumption + Gross investment + Government spending + - (Exports-Imports). GDP = C+I+G+ (X-M).

Consumption: This includes personal expenditures pertaining to food, households, medical expenses, rent, etc. Gross Investment: Business investment as capital which includes construction of a new mine, purchase of machinery and equipment for a factory, purchase of software, expenditure on new houses, buying goods and services but investments on financial products is not included as it falls under savings.

Government spending : It is sum of government expenditure on final goods and services. It includes salaries of public servants, purchase of weapons for the military, and any investment expenditure by a government. It does not include any transfer payments, such as social security or unemployment benefits.

Exports: This includes all goods and services produced for overseas consumption.

Imports: This includes any goods or services imported for consumption and it should be deducted to prevent from calculating foreign supply as domestic supply.

Income Approach: As per this method, GDP is the sum of the following major components: (i) Compensation of employees (ii) Property income (iii) Production taxes and depreciation on capital.

Compensation of Employees : It represents wages, salaries, and other employee supplements.

Property Income: It constitutes corporate profits, proprietor's incomes, interests, and rents.

Product Approach: As per this method, GDP is the value of final goods produced in the economy.

Real GDP or GDP at constant price: It is the value of today's output at some base year. Real GDP is calculated by tracking the volume or quantity of production after removing the influence of changing prices or inflation. It reflects the real growth.

Nominal GDP or GDP at current prices: represents the total money value of final goods and services produced in a given year, where the values are expressed in terms of the market prices of eduh year. Simply it is the value of today's output at today's price.

=QC

GDP at market prices measures the value of output at market prices after adjusting for the effect of indirect taxes and subsidies on the prices. Market price is the economic price for which a good or service is offered in the market place.

GDP at Factor Cost measures the value of output in terms of the price of factors used in its production. Factors of production are land, labour, capital and entrepreneur they get remunerations in the form of rent, wages, salaries, interest and profits are respectively.

GDP at factor cost = GDP at market prices — (indirect taxes — subsidies).

UTILITY OF GDP CONCEPTS

1. **GDP** is an 'aggregate' measure. it does not indicate any thing about how the GDP is distributed among the population of the country. Per capita income, another derivative of GDP, also does not indicate the pattern of income distribution. Thus, a country may have high GDP but much skewed distribution of income. Such inequality in income distribution often leads to social tensions.
2. Like the inequality of income distribution among population, there could be regional disparity in GDP with a few developed states contributing the most to the country's GDP and a majority of less developed state economies contributing a meager.
3. Higher GDP does not necessarily imply higher welfare. Welfare is a wider concept which encompasses development in all aspects of the society, e.g., health, education, sanitation, etc. India has over time grown from a low GDP nation to high GDP nation, yet its social development indicators are not commensurately favourable. Therefore, interpretation of GDP should always be supplemented by_ some kind of Human Development Index (HDI) as developed by the World Bank.
4. GDP does not reflect the total income of a country if the country is an export-oriented economy like one of those South-East Asian economies. Gross National Product (GNP) is a more accurate measure in this context, as it factors in earnings from the external sector.
5. Concept like GDP does not throw light on how much of the population is financially excluded or included. Lower level of financial inclusion is today a global malady and therefore GDP measures should be evaluated accordingly.
6. One of the newest concepts in GDP today is the 'green' GDP. A country may be achieving high GDP but at the cost of its environmental degradation. Environmental issues in growth are quite pertinent and sensitive matters today. Statisticians all over the world are busy with developing models which can measure 'green' **GDP.**

NATIONAL INCOME CONCEPTS

1. In its general form the national income is total value of all the final goods and services produced in a country (economy) during one year. It is important that these goods and services are measured in terms of a common measure i.e. in terms of money. There are various concepts related with national income such as gross domestic product, net domestic product, gross national product, net national product, national income and personal income. These are explained here under:
2. **Gross Domestic Product: It** is total money value of all final goods and services produced within a country's domestic territory during a particular period. The goods should be consumer goods or capital goods but should not include intermediary goods and services.
3. *(GDP = Money value of final goods of services)*
4. **Net Domestic Product:** When, out of gross domestic product, the amount of depreciation on fixed capital used in the production process is reduced, we get net domestic product.
5. *(NDP = GDP — Depreciation)*
6. **Gross National Product:** This concept is seen **in** the context of citizenship, which means adding the net factor income from abroad to gross domestic product.
7. The net factor income from abroad can be positive or negative which would depend on as to how much wages, rent, interest and profit is earned by foreign citizens in India and Indian citizens in foreign countries.
8. *(GNP = GDP + net factor income from abroad)*
9. **Net National Product: It** can also be worked as gross national product reduced by the amount of depreciation. *(NNP = GNP Depreciation)*
10. **National Income:** National income means the net national product at factor cost, which include total of net domestic product at factor cost plus net factor income from abroad.

11. *Net domestic product at factor cost* means the total amount earned by various factors of production with in the domestic territory of a country during a particular period. The net domestic product at factor cost is the net domestic product at market price (-) indirect taxes (+) amount of subsidies given by the government.
12. *Net domestic product* at *market price* means market value of all the final goods and services produced within domestic territory of a country. In actual practice the net domestic product at factor cost and at market price are not equal although they should be equal.
    The net domestic product at market price is the net domestic product at factor cost (+) indirect taxes (-) subsidies.

Calculation of GDP — Different approaches

(1) Output approach : GDP at market price = value of output minus intermediate consumption. NNP at factor cost = GDP at market price - depreciation + NFIA (net factor income from abroad) - net indirect taxes

(2) Income approach : NDP at factor cost = Compensation of employees + Net interest + Rental & royalty Income + Profit of incorporated and unincorporated firms + Income from self-employment. (continued in the adjoining column)

National income = NDP at factor cost + NFIA (net factor income from abroad).

(3) The expenditure approach GDP = C + I + G + (X - M)

Where: C = household consumption expenditures / personal consumption expenditures.

I= gross private domestic investment

G = govt. consumption and gross investment expenditures

X = gross exports of goods and services

New Methods of Computing GDP

Central Statistical Organisation, introduced changes in computation of Gross Domestic Product in 2015. Accordingly the GDP share as per 2011-12 series for Agriculture is 19%, for Industry 32% and for Services = 49%. According to changed criteria, the headline growth is to be measured by GDP at constant market prices (to be referred as GDP), which *is* an international practice. Earlier it was measured in terms of GDP at factor cost. Sector-wise estimates of **Gross Value Added (GVA)** shall be at basic prices instead of factor cost.

GVA is an economic measurement used to calculate the productivity of an economy. The value added formula is the difference between total economic output and intermediate consumption goods. The relationship between GVA at factor cost, GVA at basic prices and GDP (at market prices) is given below:

GVA at basic prices = CE + OS / MI + CFC + production taxes less production subsidies.

GVA at factor cost = GVA at basic prices — production tax less production subsidies

Gross Domestic Product (GDP) = Summation GVA at basic prices — product tax — product subsidies

(CE = Employee compensation, OS = Operating surplus, MI = Mixed income, CFC = Consumption of fixed capital).

FORMULAE

Ministry of Statistics & Program Implementation revised the base year from 2004-05 to 2011-12 for national accounts and introduced the following formulae:

1. Gross value added (GVA) at basic prices = CE + OS/MI + CFC + Production taxes less Production subsidies
2. GVA at factor cost (earlier referred to as GDP at factor cost) = GVA at basic prices plus Production taxes less Production subsidies
3. GDP = GVA at basic prices + Product taxes - product subsidies
4. NDP/NNI = GDP/GNI CFC

S. GNI = GDP + Net primary income from ROW

6. Primary Incomes = CE + Property *and* Entrepreneurial Income
7. NNDI =NNI + other current transfers from ROW, net (Receipts less payments)
8. GNDI = NNDI + CFC = GNI + other current transfers from ROW, net (Receipts less payments)
9. Gross Capital Formation= Gross Savings+ Net Capital Inflow from ROW
10. GCE = GFCF + CIS + Valuables + Errors and Omissions

11. Gross Disposable Income of Govt = GFCE + Gross Saving of GG
12. Gross Disposable Income of Households = GNDI GDI of Govt. Gross Savings of All Corporations

Human Development Index (HDI)

UN Human Development Index (HDI) measures poverty, literacy, education, life expectancy, and other factors. It is a standard means of measuring well-being, especially child welfare. The index was developed In 1990 by the Pakistani economist Mahbub ul Maq. It is used since '1993 by the United Nations Development Program in its annual report.

HDI measures the average achievements in a country in 3 basic dimensions of human development:

1. Long & healthy life (measured by life expectancy at birth).
2. Knowledge, as measured by adult literacy rate (with two-thirds weight) and the combined primary, secondary and tertiary gross enrollment ratio (with one-third weight).
3. Decent standard of living, as measured by GDP per capita (Purchasing Power Parity In $US).

Each year, countries are ranked according to these measures. HDI Is considered by many to be an excellent tool for measuring development, since both economic and social indicators are covered.

Value - HDI can have a value between 0 and 1. Nearer It is to 1, higher the level of human development. Countries and regions have classified into four categories:

1. Low human development: <0.535
2. Medium human development: from 0.535 to 0.710
3. High human development: 0.711 to 0.800
4. Very high human development >0.801

National Institution for Transforming India (NITI)

National Institution for Transforming India or NITI Aayog is a policy think-tank of Government of India that replaces Planning Commission.

Government of India had announced formation of NITI Aayog on 1 January 2015. The Planning Commission was strapped on Aug 13, 2014.

Members : The NM Aayog comprises the following:

1. Prime Minister of India as the Chairperson;
2. Governing Council, comprising the Chief Ministers of all the States and Union Territories with legislature and Lieutenant Governors of other Union Territories;
3. Regional Councils will be formed to address specific issues and contingencies impacting more than one State or a Region. These will be formed for a specified tenure. These Councils will be convened by the Prime Minister and will consist of the Chief Ministers of States and Lt. Governors of Union Territories in the region. These will be chaired by the Chairperson of the NITI Aayog or his nominee.

4.Experts, specialists and practitioners with relevant domain knowledge as special invitees nominated by the Prime Minister;

5. Full-time organizational framework (in addition to Prime Minister as the Chairperson) comprising:

1. Vice-Chairperson;
2. Two full time Members;
3. Part-time members: Maximum of two from leading universities research organizations and other relevant institutions in an ex-officio capacity. Part-time members will be on a rotational basis.

4. Ex Officio members: Maximum of four members of the Union Council of Ministers to be nominated by the Prime Minister;

5. Chief Executive Officer: To be appointed by the Prime Minister for a fixed tenure, in the rank of Secretary to the Govt of India.
6. Secretariat as deemed necessary.

Present Set-up: CEO - Sindhushree Khuilar, Vice Chairperson - Arvind Panagariya,Ex-Officio Members - Rajnath Singh, Arun Jaitley, Suresh Prabhu and Radha Mohan Singh, Special Invitees - Nitin Gadkari, Smriti Zubin Irani and Thawar Chand Gehlot and Full-time Members - Bibek Debroy Et V. **K.** Saraswat

Aims and Objectives of NIT! Ayog

NITI Aayog seeks to provide a critical directional and strategic input into the development process.

- The Centre-to-State, one-way flow of policy, in the Planning Commission era, is to be replaced by a genuine and continuing partnership of states..

NITI Aayog emerge as a "think-tank" that will provide Governments with relevant strategic and

technical advice across the spectrum of key etementspf policy.

- The NITI Aayog will also seek to put an end to the stow implementation of policy, by fostering better Inter-Ministry coordination and better Centre-State coordination.
- It will help evolve a shared vision of national development priorities, and foster cooperative federalism, recognizing that strong states make a strong nation.
- The NITI Aayog will develop mechanisms to formulate credible plans to the village level and aggregate these progressively at higher levels of government.
- It will ensure special attention to the sections of society that may be at risk of not benefitting adequately from economic progress.

PURCHASING POWER PARITY

When GDP per capita, for all countries is measured in the one currency say the US dollars, it may provide a misleading picture of how welloff, the people in different countries are, because the exchange rates don't reflect the purchasing power of currencies within their own economies. Purchasing power parity tries to equate currencies in terms of what they can buy in their domestic economies. For example one US dollar worth Rs.45 in India may be able to buy 'more goods in India in comparison *to* what a dollar in US would be able to buy. If ten rupees in India could buy roughly what a dollar in US can, India's GDP when ex-pressed in US dollars using the PPP principle, would increase almost 4.5-fold from the level suggested using nominal exchange rate.

UNION BUDGET

Receipts:

1. Receipts include Revenue Receipts and Capital Receipts.
2. Revenue Receipts include (i) Tax Revenue (ii) Non Tax Revenue.
3. Capital Receipts include (i) Non Debt Receipts (ii) Debt Receipts.
4. Tax Revenue: (i) Corporation tax (ii) Income Tax (iii) Other taxes and Duties (iv) Customs (v) Union Excise Duties (vi) Service Tax (vii) Taxes of the Union Territories
5. Net Tax Revenue: Gross tax revenue (-) NCCD transferred to the National Calamity Contingency Fund"(-) States' Share
6. Non-Tax Revenue: (i) Interest Receipts (ii) Dividend and Profits (iii) External Grants (iv) Other Non-Tax Revenue (v) Receipts of Union Territories.
7. Total Revenue Receipts: Net Tax Revenue + Total Non- Tax Revenue
8. Capital Receipts: Non-debt Receipts + Debt Receipts
9. Non-debt Receipts: (i) Recoveries of Loans & Advances (ii) Miscellaneous Capital receipts
10. Debt Receipts: (i) Market Loans (ii) Short Term Borrowings (iii) External Assistance (Net) (iv) Securities Issued against Small Savings, (v) State Provident Funds (Net) (vi) Other Receipts (Net)
11. Total Receipts: Total Revenue Receipts + Capital Receipts + Drawdown of Cash balance.
12. Financing of Fiscal Deficit: Debt Receipts + Draw-Down of Cash Balance

Expenditure:

1. Expenditure includes Non Plan expenditure and Plan expenditure:
2. Non Plan expenditure includes Revenue Non plan Expenditure and Capital Non Plan Expenditure.
3. Revenue Non Plan Expenditure includes (i) Interest Payments and Prepayment Premium (ii) Defence (iii)
   Subsidies (iv) Grants to state and **U.T.** Governments (v) Pensions (vi) Police (vii) Assistance to States from National Calamity Contingency Fund (viii) Economic Services (Agriculture, Industry, Power, Transport, Communications, Science & Technology etc.) (ix) Other General Services (Organs of State, Tax Collection, External Affairs etc.) (x) Social Services (Education, Health, Broadcasting, etc) (xi) Postal Deficit (xii) Expenditure of Union Territories without Legislature (xiii) Amount met from Natibnal Calamity Contingency Fund (xiv) Grants to Foreign Government
4. Capital Non Plan Expenditure includes (i) Defence (ii) Other Non-Plan Capital Outlay (iii) Loans to Public Enterprises (iv) Loans to State and U.T. Governments (v) Loans to Foreign Governments

(vi) Others

5. Plan Expenditure: includes Revenue expenditure and Capital expenditure.
6. Revenue Expenditure includes Central Plan and Central Assistance for State & Union Territory Plans
7. Capital Expenditure includes Central Plan and Central Assistance for State & Union Territory Plans
8. Total Expenditure: Total Non-Plan Expenditure + Total Plan Expenditure
9. Deficit Concepts:

- Revenue deficit is the excess of revenue expenditure over revenue receipts.
- Gross fiscal deficit is the excess of total expenditure including loans, net of recoveries over revenue receipts (including external grants) and non-debt receipts.
- Net fiscal deficit is the difference between gross fiscal deficit and net lending.
- Net primary deficit denotes net fiscal deficit minus net interest payments.
- The net RBI credit to the Central Government is the sum of increase in the Reserve Bank's holding of i) Treasury Bills, ii) Government of India dated securities iii) rupee coins and iv) Loans and Advances from the Reserve Bank to centre since Aprill, 1997 adjusted for changes in Center's cash balances with the Reserve Bank.

TERMS USED IN THE BUDGET

a Revenue receipts - Receipts by way of direct and indirect taxes, interest, dividends and profits from investments, fees and other receipts from services rendered by the Govt.

b Capital receipts - Receipts by way of loans raised from the market, borrowing from RBI, external assistance from foreign Govts, recoveries of loans and advances.

c Revenue expenditure - These are expenses incurred for the normal running of the Govt. departments, interest charges on debt and subsidies.

d Capital expenditure - It is the expenditure incurred on acquisition of assets and investments, loans and advances to State Govts.

Capital budget - It consists of capital receipts and payments and also incorporates transactions in the Public Account.

e Plan expenditure

It is the outlay on schemes and programmes formulated by various Ministries under the 5-year plan.

f Non-plan expenditure

It is the expenditure outside that incurred in keeping with the programmes formulated under the 5-year plan.

g Revenue deficit - It is the excess of Govt. revenue expenditure over revenue receipts.

h Budgetary deficit : It is excess of total expenditure (capital and revenue) over total 'receipts, bridged through borrowings from the market and RBI.

i Fiscal deficit : It is excess of total expenditure over revenue receipts and capital receipts after excluding borrowing

j Primary deficit - It is the fiscal deficit reduced by expenditure on interest payment.

k Consolidated fund : All revenues received by government, loans raised by it and receipts from recoveries of loans granted by it, form the consolidated fund. While all expenditure of the Govt. is incurred from the consolidated fund, no amount can be withdrawn from the fund without authorisation from Parliament.

l Contingency fund : Occasions may arise when government may have to meet urgent unforeseen expenditure pending authorisation from Parliament. The contingency fund is an imprest placed at the disposal of the President to incur such expenditure. Parliamentary approval for such expenditure and for withdrawal of an equivalent amount from the fund is subsequently obtained and the amount spent from the fund is recouped to the Fund. The corpus of the fund authorised by the Parliament, at present, is Rs.50 cr.

m Zero Based Budget (ZBB) : begins with decision units that are the lowest levels in the organisation for which a budget is prepared. A set of decision packages is prepared for each unit, which basically describes various levels of service, that may be rendered by the decision unit. The frequently mentioned benefits of ZBB is the increased participation of managers in the budget-making process.

n Demands for grants: This is the form in which estimates of expenditure included in the annual financial statement and required to be voted in the Lok Sabha, are submitted. Generally one demand

for grant is presented in respect of each ministry or department.

- **Appropriation bill:** After the demands for grants are voted, the Parliament's approval to the withdrawal from the Consolidated Fund of the amounts so voted and the amount to meet the expenditure charged on the Consolidated fund, is sought through the Appropriation Bill.

UNION BUDGET 2015-2016

KEY FEATURES

Three Key achievements

1. Financial Inclusion - 12.5 crores families financially mainstreamed in 100 days.
2. Transparent Coal Block auctions to augment resources of the States.
3. Swachh Bharat is not only a programme to improve hygiene and cleanliness but has become a movement to regenerate India.
4. Game changing reforms on the anGil: (a) Goods and Service Tax (GST); (b) Jan Dhan, Aadhar and Mobile (JAM) - for direct benefit transfer.

STATE OF ECONOMY

Inflation: CPI inflation projected at 5% by the end of the year, consequently, easing of monetary policy. Monetary Policy Framework Agreement with RBI, to keep inflation below 6%.

GDP Growth: Based on the new series, estimated GDP growth for 2014-15 is 7.4%.Growth in 2015-16 is expected to be between 8 to 8.5%.

Amrut Mahotsav - The year 2022, 75th year of Independence Vision for "Team India" led by led by the States and guided by the Central Government

1. Housing for all - 2 crore houses in Urban areas and 4 crore houses in Rural areas.
2. Basic facility of 24x7 power, clean drinking water, a toilet and road connectivity.
3. At least one member has access to means for livelihood.
4. Electrification of the remaining 20,000 villages including off-grid Solar Power- by 2020.
5. Connecting each of the 1,78,000 un-connected habitation.
6. Providing medical services in each village and city.
7. Ensure a Senior Secondary School within 5 km reach of every child, upgrade over 80,000 secondary schools and add or upgrade 75,000 junior/middle, to the senior secondary level. Improving quality of education and learning outcomes.
8. To strengthen rural economy - increase irrigated area, improve the efficiency of existing irrigation systems, and ensure value addition and reasonable price for farm produce.
9. Ensure communication connectivity to all villages.
10. To make India, the manufacturing hub of the World through Skill India and the Make in India Programmes.
11. Encourage and grow the spirit of entrepreneurship - to turn youth into job creators.
12. Development of Eastern and North Eastern regions on par with the rest of the country.

Major Challenges Ahead: Agricultural income under stress, increasing investment in infrastructure, decline in manufacturing from 18% to 17% of GDP as per new GDP data; and manufacturing exports have remained stagnant at about 10% of GDP, resource crunch in view of higher devolution of 42% share of the divisible pool of taxes to States (total transfer to the States will be about 62% of the total tax receipts of the country), maintaining fiscal discipline. To meet these challenges public sector needs to step in to catalyse investment, make in india programme to create jobs in manufacturing, continue support to programmes with important national priorities such as agriculture, education, health, MGNREGA, rural infrastructure including roads. Challenge of maintaining fiscal deficit of 4.1% of GDP met in 2014-15, despite lower nominal GDP growth due to lower inflation and consequent sub-dued tax buoyancy.

Fiscal Roadmap: Government firm on journey to achieve fiscal target of 3% of GDP. With improved economy, pressure to accelerate fiscal consolidation too has decreased. Accordingly, journey for fiscal deficit target of 3% will be achieved in 3 years rather than 2 years. The fiscal deficit targets are 3.9%, 3.5% and 3.0% in FY 2015 16, 2016-17 & 2017-18 respectively. Additional fiscal space will go to funding infrastructure investment. Need to view public finances from a National perspective and not just the perspective of the

Central Government. Aggregate public expenditure of the Governments, as a whole can be expected to rise substantially. Disinvestment to include both disinvestment in loss making units, and some strategic disinvestment.

Good governance: Need to cut subsidy leakages, not subsidies themselves. To achieve this, Government committed to the process of rationalizing subsidies. Direct Transfer of Benefits to be extended further with a view to increase the number of beneficiaries from 1 crore to 10.3 crore

GDP for BE 2015-2016 has been projected at Rs. 14108945 crore assuming 11.5% growth over the Advance Estimates of 2014-2015 c 12653762 crore) released by CSO. Fig in bracket are percentage of GDP.

Major Highlights

Fiscal Roadmap

Journey for fiscal deficit target of 3% will be achieved In 3 years rather than 2 years. The fiscal deficit targets are 3.9%,

3.5% and 3.0% in FY 2015-16, 2016-17 & 2017-18 respectively.

- Additional fiscal space will go to funding infrastructure investment.

Govt. Schemes Allocation : MNREGA Rs.34699 cr, NRLM and NULM Rs.3343 cr, Housing Rs.14200 Cr, PMG Sark Yojna Rs.14291, Swachh Bharat Yojna Rs.6000 cr, Krishi Unnoti Yojna Rs.12257, Sary Sikhsha Abhiyan R.s.22000 c, Mid-day Meal Rs.8900 cr, National Health Mission Rs.18000 cr.

Agriculture

- 'Paramparagat Krishi Vikas Yojana' to be fully supported.
- 'Pradhanmantri Gram Sinchai Yojana". (PMKSY) to provide 'Per Drop More Crop'. Rs.5,300 crore to support micro-irrigation, watershed development and PMKSY.
- Rs.25,000 crore in 2015-16 to the corpus of Rural Infrastructure Development Fund set up in NABARD; Rs.15,000 crore for Long Term Rural Credit Fund; Rs.45,000 crore for Short Term Co-operative Rural Credit Refinance Fund and R.s.15,000 crore for Short Term RRB Refinance Fund.
- Target for short term agriculture credit : Rs.8.5 lakh crore.
- Government to work with the States, in NITI, for the creation of a Unified National Agriculture Market. Funding the Unfunded
- Micro Units Development Refinance Agency (MUDRA) Bank, with a corpus of Rs.20,000 crores and credit guarantee corpus of Rs.3,000 crores to be created.
- In lending, priority will be given to SC/ST enterprises.
- MUDRA Bank will refinance all Micro-finance Institutions in the business of lending to such small entities of business through a Pradhan Mantri Mudra Yojana.
- A Trade Receivables discounting System (TReDS) which will be an electronic platform for facilitating financing of trade receivables of MSMEs to be established.
- Comprehensive Bankruptcy Code of global standards to be brought in fiscal 2015-16 towards ease of doing business.
- Postal network (154000 points) spread across villages to be used for increasing access to the formal financial system.
- NBFCs registered with RBI and having asset size of Rs.500 crore and above may be considered for notifications as 'Financial Institution' in terms of the SARFAESI Act, 2002. Infrastructure
- National Investment and Infrastructure Fund (NIIF), to be established with an annual flow of Rs.20,000 crores to it.
- Atal Innovation Mission (AIM) to be established in NITI to provide Innovation Promotion Platform involving academicians, and drawing upon national and international experiences to foster a culture of innovation, research and development. A sum of Rs.150 crore will be earmarked.
- (SETU) Self-Employment and Talent Utilization to be established as Techno-financial, incubation and facilitation program to support all aspects of start-up business. Rs.1000 crore to be set aside as initial amount in NITI.
- 5 new Ultra Mega Power Projects, each of 4000 MW, in the Plug-and-Play mode. Financial Market
- Provision for Recapitalization of PS banks Rs.7940 cr, Exim Bank Rs.1300 cr, NABARD Rs.300 Cr and

SIDBI for CGF for Factoring Rs.250 cr, made for 2015-16.

- Public Debt Management Agency (PDMA) bringing both external and domestic borrowings under one roof to be set up this year.
- Forward Markets commission to be merged with SEBI.
- Section-6 of FEMA to be amended through Finance Bill to provide control on capital flows as equity will be exercised by Govt. in consultation with RBI.
- India Financial Code to be introduced soon in Parliament for consideration. **Monetising Gold**
- Gold monetisation scheme to allow depusitors of gold to earn interest in their metal accounts and jewellers to obtain loans in their metal account to be introduced.
- Sovereign Gold Bond (alternative to metal gold) scheme to be developed.
- Indian Gold Coin to be developed which will carry the Ashok Chakra on its face. Skill India
- A national skill mission to consolidate skill initiatives spread accross several ministries to be launched.
- DD Upadhyay Gramin Kaushal Yojana to enhance the employability of rural youth.
- A student Financial Aid Authority to administer and monitor the front-end all scholarship as well Educational Loan Schemes, through the Pradhan Mantri Vidya Lakshmi Karyakram, to be established.
- New All India Institute of Medical Science (AIIMS) to be set up in I&K, Punjab, Tamil Nadu, Himachal Pradesh and Assam.
- An autonomous Bank Board Bureau to be set up to improve the governance of public sector bank. TAX PROPOSAL
- Efforts on various fronts to implement GST from 1.4.2016.
- No change in rate of personal income tax.
- Proposal to reduce corporate tax from 30% to 25% over the next four years, starting from next financial year.
- Exemption to individual tax payers to continue to facilitate savings.

Black Money

structure of electronic filing of statements by reporting entities to ensure seamless integration of data for more effective enforcement. Bill for a comprehensive new law to deal with black money parked abroad to be introduced in the current session. •

swachh Bharat

- 100% deduction for contributions, other than by way of CSR contribution, to Swachh Bharat Kosh and Clean Ganga
- **CF** energy cess increased from Rs.100 to Rs.200 per metric tonne of coal, etc. to finance clean environment initiatives.

  Enabling provision to levy Swachh Bharat cess at a rate of 2% or less on all or certain services, if need arises.

Benefits to middle class tax-payers

- Limit of deduction of health insurance premium increased from Rs.15000 to Rs.25000, for senior citizens limit increased from Rs.20000 to Rs.30000.

  Senior citizens above the age of 80 years, who are not covered by health insurance, to be allowed deduction of Rs.30000 towards medical expenditures.
- Deduction limit of Rs.60000 with respect to specified decease of serious nature enhanced to Rs.80000 in case of senior citizen.
- Additional deduction of Rs.25000 allowed for differently abled persons.
- Limit on deduction on account of contribution to a pension fund and the new pension scheme increased from Rs.1 lakh to Rs.1.5 lakh.
- Additional deduction of Rs.50000 for contribution to the new pension scheme u/s BOCCD.
- payments to the beneficiaries including interest payment on deposit in Sukanya Samriddhi scheme to be fully exempt.
- Service-tax exemption on Varishtha Bima Yojana.
- Conversion of existing excise duty on petrol and diesel to the extent of Rs.4 per litre into Road Cess to fund investment. Negative List under service-tax is being slightly pruned to widen the tax base.

. Yoga to be included within the ambit of charitable purpose under Section 2(15) of the Income-tax Act.

CHALLENGES FACING INDIAN ECONOMY

There are five challenges facing Indian Economy in the current context. These are given below:

1. Timing of exit from the accommodative monetary policy in the context of rising food price-led inflation but still weak growth;
2. The possibility of another surge in capital flows, especially if we turn out to be an outlier in withdrawal of monetary stimulus;
3. Monetary transmission mechanism as it is evolving from the crisis period;
4. Return to fiscal consolidation and quality of fiscal adjustment;
5. The implications of the efforts towards financial stability on financial inclusion and growth.

Unique features of Indian Economy

1. Our growth is driven by domestic demand — both consumption and investment. Consumption and saving are well balanced. In India, the share of private final consumption expenditure in GDP is around 55 per cent. Our savings rate is 37.7 per cent and investment rate is 39.1 per cent.
2. Twin deficits — fiscal as well as current account deficit. India was on a path of fiscal consolidation before the crisis, but got off track because of the counter cyclical spending necessitated by the crisis. Unlike major EMEs, which are running current account surpluses, we have recorded deficits on the current account. Although current account deficits have been modest, the deficit reached a high of 2.6 per cent of GDP in 2008-09 but is expected to moderate during 2009-10.
3. Given the right balance between domestic consumption and saving on the one hand, and infrastructurel bottlenecks in major areas (such as power, roads, urban infrastructure as also social infrastructure) on the other, India is essentially a supply-constrained economy. Just before the crisis, such supply concerns led to a view that there might be overheating in the economy. Generally, weak external demand has led to some externally induced cyclical slowdown. However, as the global economy recovers, supply constraints are again expected to be binding. .

ECONOMICS TERMS

1. Closed Economy - An economy having no economic relations with the rest of the world i.e. it doesn't have trade, financial or investment relations with other countries.

2. Open Economy : An economy having economic relations with the rest of the world, i.e. it has trade, financial and investment relations with other countries.

3. National Income : It refers-to the money value of all goods and services produced within the domestic territory of a country plus net factor Income from abroad in a year.

4. Per capita income : It refers to the average income of a resident of a country and is calculated by dividing the national income by the population of the country.

5. Gross Domestic Product (GDP) : It is the money value of all final goods and services produced in the domestic territory of country in a year.

6. Net Domestic Product : obtained by reducing consumption of fixed capital (depreciation) from the GDP.

7. Gross National Product (GNP) : It is calculated by adding net factor income from abroad (NFIA) to GDP.

8. Law of Demand: It states that other things being equal, more of a commodity is demanded at a lower price and less of it at a higher price.

9. Elasticity of Demand : It is the responsiveness of a demand to a change in a any factor of demand.

10. F

actors affecting elasticity of Demand : (a) Nature of Commodity (b) Availability of substitute goods (c) Share in the total expenditure (d) Diverse uses of the commodity (e) Consumer's behaviour etc.

11. Supply curve: A graph of the relationship between the price of a good and the amount supplied at different prices

12. Consumer surplus: The difference between what a consumer would be willing to pay for a good or service and what that consumer actually has to pay.

13. **Sunk costs:** When what is done cannot be undone. Sunk costs are costs that have been incurred and cannot be reversed.
14. **Marginal Cost :** It is the addition to the total cost as a result of unit increase in production.
15. **Propensity to Consume:** The relationship between change in income and the resultant change in consumption.
16. **Fiscal Measures :** Measures to correct excess /deficient demand thorugh budget proposals of government are called fiscal measures. These include tax changes, increase /reduction in government expenditure etc.
17. **Fiscal Policy:** Fiscal policy is that part of government economic policy which deals with taxation, expenditure, borrowing, and the management of public debt in the economy.
18. **Fiscal deficit** is the gap between the government's total spending and the sum of its revenue receipts and non-debt capital receipts. It represents the total amount of borrowed funds required by the government to completely meet its expenditure
19. **Budget Deficit:** Budget may take a shape of deficit when the public revenue falls short to public expenditure. Budget deficit is the difference between the estimated public expenditure and public revenue. The government meets this deficit by way of printing net currency or by borrowing.
20. **Primary Deficit:** Fiscal Deficit minus Borrowings.
21. **Inflation: A** situation of a steady and sustained rise in general prices is usually known as inflation. Inflation is a state in which the value of money is falling i.e. prices are rising.
22. **Cost-push Inflation: It** arises due to an increase in production cost. Such type of inflation is caused by three factors: (i) an increase in wages, (ii) an increase in the profit margin and (iii) imposition of heavy taxation.
23. **Deflation:** Deflation is the reverse case of inflation. Deflation is that state of falling prices which occurs at that time when the output of goods and services increases more rapidly than the volume of money in the economy. In the deflation the general price level falls and the value of money rises.
24. **Recession: A** period of slow or negative economic growth, usually accompanied by rising unemployment.
25. **Stagnation: A** prolonged recession, but not as severe as a depression.
26. **Disinflation: A** fall in the rate of inflation. This means a slower increase in prices but not a fall in prices.
27. **Depression: A** prolonged recession in economic activity. The textbook definition of a recession is two consecutive quarters of declining outpur. A depression is an even deeper and more prolonged slump.
28. **Duopoly: A** market structure in which two producers of a commodity compete with each other.
29. **Monopoly A** market situation **in** which a product that does not have close substitutes is being produced and sold by a single seller.
30. **Perfect competition A** market situation characterized by the existence of very many buyers and sellers of homogeneous goods or services with perfect knowledge and free entry so that no single buyer or seller can influence the price of the good or service.
31. **Buyer's market: A** market in which supply seems plentiful and prices seem low; the opposite of a seller's market.
32. **Tax haven: A** country or designated zone that has low or no taxes,
33. **Tax avoidance:** A legal action designed to reduce or eliminate the taxes that one owes.
34. **Tax evasion: An** illegal strategy to decrease tax burden by underreporting income, overstating deductions, or using illegal tax shelters.
35. **Monetary policy:** The regulation of the money supply and interest rates by a central bank in order to control inflation and stabilize currency.
36. **HDI:** HDI (Human Development Index) is a composite index measuring average achievement in three basic dimensions of human life-a long and healthy life, knowledge and a decent standard of living.
37. **Engel's Law:** This law was formulated by Ernst Engel. This law states that, with given taste and preference, the portion of income spend on food diminishes as income increases. According to this law, smaller a person's income, the greater the proportion of it that he will spend on food and vice versa.
38. **Giffin Goods:** Giffin goods have the positive relationship between price and quantity demanded and as a result demand curve of Giffin goods slopes upward from left to right.
39. **Gresham's Law:** Bad money (if not limited in quantity) drives good money out circulation

40. Laffer Curve: It represents relationship between total tax revenue and corresponding tax rates.
41, **Lorenz Curve:** The Lorenz curve is a graphical representation of the cumulative distribution function of a probability distribution. This curve shows the degree of inequalities of a frequency distribution in a graphical manner.
42. Pareto efficiency: A situation in which nobody can be made better off without making somebody else worse off.
43. Pigou effect: A fall in the price level increases the real value of people's savings making them feel wealthier and thus causing them to spend more. This increase in demand can lead to higher employment
44. Okun's Law: A relationship between an economy's GDP gap and the actual unemployment rate. The relationship is represented by a ratio of 1 to 2.5. Okun found that an annual 2.5% increase in the rate of real growth above the trend growth results in a 1% decrease in the rate of unemployment.
45. Philips Curve: Inflation and unemployment have a stable and inverse relationship. The theory states that with economic growth comes inflation, which in turn should lead to more jobs and less unemployment.
46. Say's Law: Supply creates its own demand.
47. Real exchange rate: An exchange rate that has been adjusted to take account of any difference in the rate of inflation in the two countries whose currency is being exchanged.
48. Real interest rate: The interest rate less the rate of inflation.
49. Tobin tax: A proposal to reduce speculative cross-border flows of capital by levying a small tax on foreign exchange transactions.
50. Predatory pricing: Charging low prices now so you can charge much higher prices later.
51. PPP: Purchase Power Parity is the exchange rate that equates the price of a basket of identical traded goods and services in two countries.
52. Crowding out: When the state does something it may discourage, or crowd out, private-sector attempts to do the same thing. At times, excessive Government borrowing has been blamed for low private-sector borrowing.
53. Currency board: A means by which some countries try to defend their currency from speculative attack. A country that introduces a currency board commits itself to converting its domestic currency on demand at a fixed exchange rate.
54. Currency peg: When a Government announces that the exchange rate of its currency is fixed against another currency or currencies.
55. Dumping: Selling something for less than the cost of producing it.
56. Fiscal drag: is the tendency.of revenue from taxation to rise as a share of GDP in a growing economy.
57. Fiscal neutrality: When the net effect of taxation and public spending is neutral, neither stimulating nor dampening demand
58. Hard currency: A hard currency is expected to retain its value, or even benefit from appreciation, against softer currencies.GLOSSARY OF ECONOMIC TERMS
59. Aggregate demand is the sum of **all** demand in an economy. This can be computed by adding the expenditure on consumer goods and services, investment, and not exports (total exports minus total imports).
60. Aggregate supply is the total value of the goods and services produced in a country, plus the value of imported goods less the value of exports.
61. Base year: In the construction of an index, the year from which the weights assigned to the different components of the index is drawn. **It** is conventional to set the value of an index in its base year equal to 100.
62. Boom: A state of economic prosperity
63. Broad sectors of an Economy : In India Primary Sector-Agriculture, Secondary Sector - Industry, Tertiary Sector-Service.
64. Capitalism : Economic system featuring private property in means of production, commodity production and profit as the guiding motivation force of production.
65. Competition : A market phenomenon indicating rivalry amongst buyers and sellers of goods or resources classified as perfect (or pure) competition and where market power is widely diffused and free mobility in and out of **the** industry exists.
66. Cost-Push Inflation : A situation of general rise in prices in which costs (payment made to factors

owners) increase faster than productivity or efficiency. Familiar examples, wage-push and profit-push inflation.

67. Centrally planned economy: An economic system in which the production, pricing, and distribution of goods and services are determined by the government rather than market forces. Also referred to as a "non market economy." Former Soviet Union, China, and most other communist nations are examples of centrally planed economy

68. Demand-Pull Inflation : A state of rising prices brought about by increase in aggregate demand in the face of short supply.

69. Depression : A phase of the business cycle in which economic activity is at a low ebb and there is unemployment/under employment of resources; prices, profits, consumption and rate of capital investment are also at a low level.

70. Economic development: The process of improving the quality of human life through increasing per capita income, reducing poverty, and enhancing individual economic opportunities.

71. Economic Growth : Rate of increase of an economy's real incomes over a period, expressed in terms of GNP or NNP as total or per capita.

72. Economic policy: A statement of objectives and the methods of achieving these objectives (policy instruments) by government, political party, business concern, etc. Some examples of government economic objectives are maintaining full employment, achieving a high rate of economic growth, reducing income

inequalities and regional development inequalities, and maintaining price stability.

73. Equilibrium Price : Price of a commodity in the market at which supply equals demand; the point of intersection of supply and demand curve; price at which a firm's profits are maximized (or losses minimized if the firm has to produce at a loss).

74. Equilibrium Quantity : Quantity of a commodity at which demand equals supply; quantity of a commodity at which a firm's profits are maximized.

75. Hyper Inflation : A situation in which general prices are rising sharply with no or little increases in output, also called 'runway' or 'galloping inflation'.

76. Inflation : Rise in the general or average price level of goods and services; consequently, a decline in the value of money-doubling of the general price level means halving the value of money.

77. Indirect tax: A tax you do not pay directly, but which is passed on to you by an increase in your expenses. For instance, a company might have to pay a fuel tax. The company pays the tax but can increase the cost of its products so consumers are actually paying the tax indirectly by paying more for the merchandise.

78. Macroeconomics The branch of economics that considers the relationships among broad economic aggregates such as national income, total volumes of saving, investment, consumption expenditure, employment, and money supply. It is also concerned with determinants of the magnitudes of these aggregates and their rates of change over time.

79. Market mechanism: The system whereby prices of commodities or services freely rise or fall when the buyer's demand for them rises or **falls** or the seller's supply of them decreases or increases.

80. Microeconomics: The branch of economics concerned with individual decision units--firms and households--and the way in which their decisions interact to determine relative prices of goods and factors of production and how much of these will be bought and sold. The market is the central concept in microeconomics.

81. Money supply: the total stock of money in the economy; currency held by the public plus money in accounts in banks. There are various measures of money supply, including M1, M2, M3 and L; these are referred to as monetary aggregates.

82. Market Economy : Economy system in which the central problems of an economy-what, how and for whom are decided by the operation of free market forces of supply and demand.

83. Mixed Economy : An economy in which both the state and the private sector co-exit; decisions on what how and for whom are made partially by the market and particularly by the state or any other public authority; many consider it essentially a transitory form.

84. Money : Anything which is acceptable in a economy as medium of exchange, measure of value, a standard for deferred payments, and a store of value; different things used as money at different times.

85. Open economy An economy that encourages foreign trade and has extensive financial and nonfinancial contacts with the rest of the world in areas such as education, culture, and technology.
86. Planned Economy : Economic system in which basic decisions in an economy are made according to a plan.
87. Price : Value of a commodity in terms of money.
88. Real Income : Purchasing power of money income; quantity of real goods and services that money income can buy; contrasted with money income.
89. Recession : Down swing of business activity in a trade cycle. Income prices, profits and employment are falling during this phase of the trade cycle.
90. Closed economy: An economy in which there are no foreign trade transactions or any other form of economic contacts with the rest of the world.
91. Direct Tax : Tax that cannot be shifted; the burden of direct tax is borne by the person on whom it is initially fixed. Examples: personal income tax, social security tax paid by employees, death tax, etc.

TEST YOURSELF : ECONOMIC ANALYSIS

PRACTICE TEST – 01

1) Micro-economic theory studies how an economy determines.
a)The price of goods **b)**The price of services **c)**The price of economic resources **d)** All of the above.
2) A producer's positively sloped supply curve for a commodity represents. **a)**In one sense a maximum and in another sense a minimum boundary of the.producer's intentions. **b)**A maximum boundary of the producer's intentions.**c)**A minimum boundary of the producer's intentions. **d)**None of the above.
3) The theory of distribution refers to: **a)**The distribution of income among various factors of the production. **b)**The distribution of income among different individuals in the economy. **c)**Both of the above **d)**None of these
4) Interest is reward for parting with liquidity according to: **a)** B. Ohlin **b)** Von Haberler **c)** J.M. Keynes **d)** Alfred Marshall
5) Economics may be divided into macro-economics and micro-economics. Among the subject matter of micro economics may be found: **a)**The nature of value in exchange.**b)**The size of a country's national income **c)**The allocation of resources among competing uses **d)** The relative prices of specific services.
6) The statement that'economics is positive and not normative' means:
a)That economics can be used to prove that capitalism is better than socialism.**b)**That economics tells us what kind of economic behaviour or policy is wholesome and what evil **c)**That economics tells policy makers which alternative to choose from among several efficient ones. **d)**That economics can only indicate consequences of policies, choices, or conditions.
7) Which of the following statements is incorrect? **a)**Micro-economics is primarily concerned with the problem of what, how and for whom to produce.**b)**Micro-economics is primarily concerned with the behaviour of individual decision making units when at equilibrium.**c)**MiCro-economics is primarily concerned with the time path and process by which one equilibrium position evolves into another **d)**Micro-economics is primarily concerned with comparative static rather dynamics.
8) Economic laws may be described as: **a)**Principles derived from analysis of price input / output determination. **b)**Generations concerning the economic behaviour of individuals and institutions.**c)**Forecasts in quantitative terms of the economic development of society.**d)**Expression of the basic features of competition.
9) The main difference between positive economics and normative economics is that the former. **a)**Discusses the ethical implications of its laws.**b)**Concerns itself only with hypotheses which can generally be tested.**c)** Is based on the value judgements of economists.**d)**Considers carefully the political significance of its laws for a democratic society.
10) Adam Singh advocates: **a)** Laissez-faire**b)** Division of Labour **c)** Both of the above **d)** None of the above
11) The term'consumer goods' is used by economists to refer to: **a)** Goods produced for consumers in a free market only.**b)** Goods other than free goods, whose use directly satisfies consumers wants.**c)** Goods produced by consumers in return for a wage.**d)** Goods which are used by consumers in order to earn their living
12) The basic characteristic of a Capitalistic economy is: **a)** Full employment **b)** The private ownership of the means of production.**c)** An absence of monopoly **d)** Large-scale production in primary industries.
13) In a free capitalist society the allocation of the factors of production among the various productive activities is determined by: **a)** The pattern of consumer's spending **b)** The traditional employment of Locals **c)** Decisions of the Government **d)** The wealth of the entrepreneurs.
14) Who believed that an automatic equilibrating mechanism of the perfectly competitive market, known as'invisible hand' tended to maximize national wealth: **a)** Adam Smith**b)** Keynes **c)** J.B. Say **d)** None of the above
15) The fundamental economic problem being faced is one of: **a)** Consumer's choice **b)** Decision-making by the government**c)** 'Multiplicity of wants and scarcity of resources.**d)** Shortage of labour.
16) Which one of the following is not directly the concern of the economist? **a)** Aid to underdeveloped countries **b)** The effect of an increase in Bank rate **c)** The choice between alternative sites for a factory **d)** The use of taxation to discourage smoking of

cigarettes.
17) The meaning of the word'economic' is most closely connected with the word: **a)** Free **b)** Scarce **c)** Unlimited **d)** Restricted
18) Which of the following is not an economic problem?
a) Deciding between extra paid work and extra leisure. **b)** Deciding between different ways of spending leisure lime . **c)** ;:eciding on the level and form of personal saving **d)** Deciding between expenditure on one good and another.
19) Which one of the following statement is not true?
a) Exchange is one method of helping to solve the basic economic problem. **b)** The basic ecolomic problem is one of choice.**c)** Choice is necessary because of Limited wants.**d)** The means to satisfy wants i.e., the factors of production, are limited.
20) Who gave scarcity definition of economics? **a)** Adam Smith **b)** Robbins **c)** Keynes **d)** J.B. Say
21) Who is known as the Father of Economics? **a)** Keynes **b)** Ricardo **c)** Adam Smith **d)** J.S. Mill
22) Many of the basic problems of economics emerge from:
a) Unlimited resources **b)** Incompetent govt. **c)** The use of limited resources to satisfy human wants **d)** Unlimited wants
23) The utility may be defined as: **a)** The power of a commodity to satisfy wants **b)** The desire for a commodity **c)** The usefulness of a commodity **d)** The necessity of a commodity
24) The utility of a commodity is: **a)** Its expected social value **b)** Its relative scarcity **c)** The extent of its practical use **d)** The degree of its fashion
25) Marginal utility curve of a given consumer is also his: **a)** Indifference curve **b)** Demand curve **c)** Supply curve **d)** Total utility curve
26) The total utility is maximum when: **a)** MU is zero **b)** AU is the highest **c)** MU is the highest **d)** MU is equal to AU
27) The law of diminishing marginal utility states that:
a) As more of a commodity is consumed total satisfaction diminishes.**b)** The more you have of a particular commodity the less you want more of it. **c)** As more units of a commodity are produced the price of the commodity will fall **d)** The consumption of further units of a commodity will bring a steady thcrease in the amount of satisfaction obtained.
28) The law of diminishing returns or increasing cost will operate at an earlier level, in agriculture than in industry because:
a) More mechanization is applicable to agriculture **b)** Agriculture is an industry where land is used extensively **c)** Less mechanization is applicable to agriculture. **d)** More labour is used in agriculture.
29) Opportunity costs are also known as: **a)** Spillover costs **b)** Alternative cost **c)** Social costs **d)** Money costs
30) An increase in the price'of a commodity, other things remaining same, results in:
a) Increase in pricing **b)** Increases in quantity supplied **c)** Increase in demand **d)** Taxes
31) Supply remaining constant, if demand increases, price will **a)** Rise **b)** Remains constant **c)** Fluctuate **d)** Fall
32) Perfect competition is said to exist if: **a)** There are homogenous products **b)** Each firm in the industry accepts the market price because it has to accept it. **c)** Price is fixed not by a firm **d)** All of the above
33) Consumer's surplus is highest in case of: **a)** Luxuries **b)** Necessities **c)** Comforts **d)** Conventional necessities.
34) A "Giffen Goods" is one for which, in response to a small change in price. **a)** A zero income effect is just outweighed by a positive substitution effect. **b)** A negative income effect is just outweighed by a positive substitution effect. **c)** A zero income effect is matched by a zero substitution effect. **d)** A negative income effect outweighed any'substitution effect.
35) Which is correct?
a) An "increase of demand" is not the same thing as an "extension of demand". **b)** An "increase of demand is the same thing as an "extension of demand". **c)** An increase of demand is just equal to the extension of demand. **d)** All the above statements are wrong e) An increase of demand invariably reduces the extension of demand.
36) Demand means:
a) The desire and willingness of an individual for all goods and services for his standard of living. **b)** The desire, ability and willingness of an individual to purchase goods and services at a given time and price **c)** Both A and B **d)** None of the above
37) The demand function for a commodity is defined as: **a)** Quantity demanded as a function of the goods, own price, the price of the substitute and the buyer's income **b)** Price of Substitutes as a functions of the goods own prices **c)**Quantity demanded as a function of tne price of other goods **d)** All the above
38) In the typical demand schedule, quantity demanded.
a) Varies directly with price.**b)** Varies proportionately with price **c)** Is independent of price **d)** Varies inversely with price
39) Law of demand states that when:
a) Income rises demand rises.**b)** Price rises demand rises.**c)** Price falls demand falls.**d)** Price falls demand rises
40) The law of demand indicates: **a)** The relationship between income and quantity demanded **b)** The relationship between price of a commodity and price of ifs substitutes **c)** The relationship between price of two commodity.**d)** The relationship between the price of commodity and the quantity demanded.
41) Which of the following conditions is required condition for the operation of law of demand? **a)** Price of subStitute change,,,**b)** Income and Taste of consumer remains constant **c)** Production does not increase **d)** Taste of the consumer change
42) Demand curve shows:
a) Inverse relationship between quiantitydemailed and its cost of production.**b)** Inverse relationship between the rate of change of demand and price.**c)** Inverse relationship between the rate of change in demand and cost of production at a given times. **d)**

Direct relationship between the demand and the price of a commodity at a given time.
43) When we say that a demand curve for a commodity slopes downwards to the right we mean: **a)** More of the commodity will be demanded as income increase **b)** More of the commodity will be demanded as the price of the substitutes falls. **c)** More of the commodity will be demanded as population rise.**d)** More of the commodity will be demanded as its own price falls.
44) A fall in the price of a commodity leads to:
a) A shift in demand **b)** A fall in demand **c)** A fall in the consumers real income **d)** A rise in the consumers real income
45) An exceptional demand curve is one that slopes: **a)** Upward to the lift **b)** Upward to the right **c)** DoWnward to the right **d)** Horizontal
46) Which one is not an exception to the Law of Demand? **a)** Ignorance**b)** Inferior good **c)** Normal good **d)** Articles of Distinction
47) Demand for a commodity is elastic when has:
a) Only one use **b)** Many Use **c)** Uses, which cannot be postponed **d)** Uses very essential for the consumer
48) Which of the following pairs of commodities is an example of substitute:
a) Coffee and milk **b)** Mustard oil and coconut oil **c)** Diamond and cow **d)** Pen and ink
49) For most customers apples and oranges are substitute goods. Therefore, we would expect a rise in the price of apples to lead to: **a)** A rightward shift in the supply curve of oranges **b)** A leftward shift in the supply curve of oranges. **c)** A fall in the price of oranges **d)** An upward change in the demand curve of oranges.
50) A change in climate ,conditions resulting in hot weather, price remaining the same, would cause a consumer of cold drinks:
a) To move to a lower curve **b)** To move lower down the demand curve **c)** To move to a higher demand curve **d)** To move up the same demand curve
51) When an individual's income falls (while everything else remains the same) his demand for an inferior goods:
a) Increase **b)** Remaining unchanged **c)** We cannot say without additional information **d)** Decrease
52) A fall in the price of a commodity whose demand curve is a rectangular hyperbola causes total expenditure on the commodity to: **a)** Remain unchanged **b)** Increase**c)** Decrease **d)** Any of the above
53) The relationship between demand for a commodity and price, ceteris paribus, is:
%**a)** Negative **b)** Positive**c)** Non-negative **d)** Non-positive
54) Other things being equal a decrease in the quantity supplied to the market at given prices leads to:
a) A higher price and a contraction of demand **b)** A higher price and an expansion of demand. **c)** A higher price and an expansion of demand **d)** A lower price and a contraction of demand.
55) Law of demand explains: **a)** Quantitative relationship between price and demand **b)** Qualitative relationship between price and demand **c)** Relationship between demand and supply **d)** Rate of change in price and demand
56) We can say with certainty that when the demand for TVs increases in the long run, prices:
a) Will go down **b)** Will go up **c)** Change proportionately **d)** Cannot be predicted with the knowledge of elasticity of demand
57) In the normal demand schedule, quantity demanded:
a) Varies directly with price **b)** Is independent of price **c)** Varies inversely with price **d)** Varies proportionately with price
58) An example of derived demand is demand for: **a)** Pen and ink **b)** Wool and mutton **c)** Petrol and Car **d)** None of the above
59) By increase in demand we mean: **a)** Movement upwards on a demand curve **b)** Movement downwards on demand curve **c)** Shifting upwards of a demand curve **d)** None of these
60) Law of demand operates because of
a) Price changes **b)** The principle of different income **c)** Changes in advertisement expenses **d)** None of the above
61) Multiple uses of a commodity will make the demand go up when:
a) Price increases **b)** Price remains the same**c)** Price falls down **d)** None of the above
62) Status symbol goods are:
a) Veblen goods **b)** Exception to law of demand **c)** Goods of conspicuous consumption **d)** ALL OF THE ABOVE
63) Price - demand relationship in the case of Giffen goods is:
a) Inverse •**b)** Direct **c)** Absent **d)** None of the above
64) The downward sloping demand curve may be partly explained by the "income effect" which refers to:
a) People's tendency to save more as their real incomes fall in the short period. **b)** An increase or decrease in the amount of a good purchased because of a price-induced change in the purchasing power of a fixed income. **c)** Changes in the relative importance of good purchased because of changes in the con imunity's tastes resulting from adverting. **d)** Changes in the distribution of income in a community.
65) The demand curve for a commodity is generally drawn on the assumption that:
a) The commodity has no substitutes **b)** Tastes, income and aii other prices remain constant. **c)** The average household consist of two persons **d)** Purchases of the commodity are made by a free market.
66) A fall in the price of a commodity leads to:
a) A shift in demand **b)** A fall in demand **c)** A rise in consumer's real income **d)** A fall in the consumer's real income.
67) In the case of Giffin good like Bajra a fall in its price tends to:

a) Make the demand remain constant **b)** Reduce the demand **c)**Increase the demand **d)**Change demand in an abnormal way.

68) Which of the following pairs of commodities is an example of substitutes:

a) Coffee and milk **b)** Diamond and cow **c)** Pen and ink **d)** Mustard oil and coconut oil.

69) For most consumers apples and oranges are substitute goods. Therefore, we would expect a rise in the price of apples to lead to: **a)** A rightward shift in the demand curve of oranges **b)** A leftward shift in the supply curve of apples **c)** A downward change in the demand curve of oranges **d)** A fall in the price of oranges

70) A change in climatic conditions resulting in hot weather, price remaining the same, would cause a consumer of cold drink: **a)** To move to a higher demand curve **b)** To move up the same demand curve **c)** To move lower down the curve **d)** To move to a lower demand curve.

71) If two goods are complementary, this means that a rise in the price of one commodity will induce: **a)** An upward shift in demand for the other commodity **b)** Arise in the price of the other commodity **c)** A downward shift in demand for other commodity **d)** No shift in demand for the other commodity.

72) If more is demanded at the same price or same quantity at a higher price, this fact of demand is known as: Extension of demand **b)** Increase of demand **c)** Contraction of demand **d)** Decrease of demand.

73) Other things being equal a decrease in demand can be caused by: A rise in the price of the commodity **a)** A rise in the income of the consumer **b)** A fall in the price of the commodity **c)** A fall in the income of the consumer

74) An increase in demand can result from: **a)** A decline in market price **b)** An increase in income **c)** A reduction in the price of substitutes **d)** An increase in the price of complementary goods **e)** All the above

75) Which of the following circumstances would be likely to bring about a change in the demand schedule for a product? **a)** A fall in the price of the product **b)** An increase in the number of potential consumers **c)** A new method of producing the product **d)** An increase in the quantity produced. **e)** Both a &b

76) If the price of good A affects the demand for good B, then: **a)** A is a substitute for B **b)** B is complement of A **c)** Changes in the price of A will cause movement along the demand schedule for A **d)** Changes in the price of B will not change the demand for A. e) Changes in the price of A will shift or change the demand for B.

77) Cross demand is the change in the quantity demanded of a given commodity in response to the: **a)** Change in the utility of another commodity **b)** Change in the price of another commodity **c)** Change in the nature of another commodity **d)** Change in the size of another commodity.

78) The law of demand states that: **a)** Demand increases with increase in income **b)** When income and prices rise. the demand also rises **c)** When income and prices rise. the demand also rises **d)** When price increases, demand increases

79) A consumer's equilibrium choice or position is one at which: **a)** His savings are maximised **b)** His assets are maximised **c)** His satisfaction is maximum **d)** Price of goods is maximised

80) For most consumers, milk and tea are substitute goods. Therefore, we should expect a rise in price of milk to lead to: **a)** A rightward shift in the supply curve of tea. **b)** A leftward shift in the supply curve of tea. **c)** A fall in the price of tea. **d)** An upward shift in the demand curve for tea.

81) Other things being equal, a fall I contraction in demand can be caused by a: **a)** Rise in prices of the substitute **a)** Rise in prices of the substitute **b)** Rise in prices of the substitute **c)** Rise in the income of the consumer **d)** Rise in the price of the commodity

82) The demand for a good is elastic if: **a)** The demand for that good increases when price falls **b)** A decrease in price results in a decrease in total expenditure **c)** The quantity demanded increases less than proportionately with the decrease in price level

83) A rightwards shifts in supply schedule indicates: **a)** A decrease in Supply **b)** A decrease in quantity supply **c)**An increase in quantity supply **d)** An increase in supply.

84) A rightwards shift in supply curve indicates: **a)** A decrease in supply **b)** An increase in quantity supplied **c)** An increase in supply **d)** None of the above

85) A supply curve will generally take an upwardsslopin9 form left to right because: **a)** Market price is normally above total costs of production. **b)** Consumers' income tend to increase in the long period. **c)** Producers' costs tend 'to increase as their output expands **d)** Supply of most goods is essentially a short-term phenomenon.

86) Other things being equal an increase in supply can cause by: **a)** A rise in the price of the commodity **b)** An improvement in the techniques of production **c)** A rise in the income of the consumer **d)** An increase in the income of the seller.

87) The shift of the supply curve for a commodity to the left may indicate, other things being equal, that: **a)** Shares in the producing firms are in great demand on the Stock Exchange. **b)** Producers of the commodity wish to make and sell less at same price. **c)** Prices raw materials used in the production of the commodity have fallen. **d)** Wages paid to the producers' employees have fallen.

88) Ceteris paribus, a decrease in quantity supplied of a commodity can be caused by: **a)** A fall in its price **b)** Fall in income **c)** Rise in price **d)** Fall in raw material

89) The supply schedule for a commodity is usually assumed to be directly open to influence by all the following except:
a) The quantity demanded **b)** The prices of the factors of production **c)** The costs of production **d)** The prices of other goods
90) Which of the following could explain why the supply curve for a commodity slopes downwards?
a) Producers do not like increasing production. **b)** Producers have to lower price to induce consumers to buy more **c)** Costs fall as production increases **d)** Diminishing marginal utility is in operation
91) "Free Trade Area" denotes: **a)** Pitlicy of Laissez faire **b)** A group of countries which have decided to impose no duties of any kind on imports from other members of the group **c)** Free Exports & Imports **d)** All the above
92) Temporary control of inflation can be effected by:
a) Lowering Bank Rate **b)** Purchasing of securities by RBI **c)** Restraint on the growth of money supply **d)** None of these
93) The term "hyper-inflation" is used to denote: **a)** Creeping inflation **b)** Step by step inflation **c)** A "Runaway" or "galloping" inflationary situation where the monetary unit becomes almost worthless **d)** None of these
. **94)** In calculating a country's GNP at market prices one of the following is not included:
a) Depreciation **b)** Net factor income from abroad **c)** Net indirect taxes **d)** Transfer Payment
95) Indian Economy can be best described as:
a) Developed economy **b)** Undeveloped economy **c)** Developing economy **d)** Underdeveloped
96) The term "balance of trade" means: **a)** Difference between exports & imports **b)** Net Exports including merchandise **c)** The difference between the cost of the imports and exports of a country. **d)** a and c
97) The open market operations refer to the sale and purchase by the RBI of:
a) Foreign exchange **b)** Gold **c)** Government securities **d)** All c' the above
98) At full employment level, which of the following would be most likely to lead to inflation?
a) A fall in taxation with no changes in gevemment expenditure **b)** An increase in productivity without any increase in wages **c)** A fall in investment with no change in prosperity to consumer **d)** A rise in the prosperity to save with no change in investment
99) Deflation is: **a)** Deficit budget **b)** Reduction in taxation **c)** Contraction in volume of money or credit that results in a decline of price level **d)** Increase in public expenditure
100) Bank rate means: **a)** Interest rate charged by moneylenders, **b)** Interest rate charged by the scheduled banks **c)** Rate of profit of the banking institution **d)** The official rate of interest charged by the central bank of the country Micro-economic theory studies how an economy determines.

ANSWER

1	D	2	A	3	A	4	C	5	D	6	D	7	A	8	B	9	B	10	C
11	B	12	B	13	A	14	C	15	C	16	C	17	C	18	B	19	C	20	B
21	C	22	C	23	A	24	B	25	B	26	A	27	B	28	B	29	B	30	B
31	A	32	D	33	B	34	B	35	A	36	B	37	A	38	D	39	D	40	D
41	B	42	B	43	D	44	D	45	B	46	C	47	B	48	B	49	D	50	C
51	D	52	A	53	A	54	D	55	C	56	D	57	C	58	D	59	C	60	A
61	C	62	D	63	B	64	B	65	B	66	C	67	B	68	D	69	A	70	A
71	C	72	B	73	D	74	B	75	E	76	E	77	B	78	C	79	C	80	D
81	D	82	C	83	D	84	C	85	C	86	D	87	B	88	A	89	A	90	C
91	B	92	C	93	C	94	D	95	C	96	D	97	D	98	A	99	C	100	D

PRACTICE TEST – 02

1) In the Keynes model above, which is independent:
a) Investment **b)** Consumption **c)** National income **d)** Consumption and investment
2) How many motives for demanding money has been given by Keynes: **a)** 1 **b)** 2 **c)** 3 **d)** 4
3) Recession is associated with fall in: **a)** Demand **b)** Supply **c)** Disinvestment **d)** Investment
4) Devaluation means: **a)** Fall in Marginal utility of Money **b)** Fall in printing of currency **c)** Risk in black money **d)** Fall in the value of money in terms of foreign currency
5) Acute inflationary situation: **a)** Makes savings in the form of bank deposits less attractive **b)** Makes savings more attractive **c)** Arises due to liquidity trap **d)** All the above
6) Inflation means: **a)** Increase in price **b)** Decrease in value of money **c)** Boom **d)** All of the above
7) The problem of unemployment in rural areas is mainly due to: **a)**Seasonal and under employment **b)** Frictional unemployment **c)** Structural unemployment **d)** Technical Lriernpleyrnent
8) NNP for a given year can be defined as: **a)** Market value of final goods only **b)** The market value of all final goods and services **c)** The market value of all final services only **d)** None of the above

9) LiqUidity preference is the term, which is used to refer to: **a)** The Reserve Bank of India's shareholdings in other financial institutions **b)** The extent to which investors prefer to keep their assets in money **c)** The community's preference for a gold-backed currency **d)** An inducement to save.
10) Which of the following are among the major determinants of the interest rate in the Keynesian theory?
a) People's desire to hold money and to keep their wealth in liquid form **b)** The available stock of money **c)** The intensity of speculation on the stock exchange **d)** The value of gold and silver on the world's markets
11) The famous book written by J.M. Keynes is entitled: **a)** Principles of Economics **b)** Law of Markets **c)** The General Theory of Employment, Interest and Money **d)**None of the above.
12) To a layman, investment means putting his money in a financial asset like bonds, fixed deposit etc. What does it mean to an economist:
a) Purchase of machines **b)** Stock of durable goods **c)** Purchase of real capital assets **d)** All of the above
1**3)** The liquidity preference arises due to:
a) Transaction Motive **b)** Precautionary Motive **c)** Speculative Motive **d)** All of these
14) Liquidity trap is likely to result when: **a)** Rate of Interest at its lowest **b)** Rate of Interest at its highest **c)** No change in supply of money **d)** When an increase in the supply of money fails to reduce the rate of interest
15) Which theory is called the Neo-Classical theory of rate of interest?
a) Risk Theory **b)** Liquidity Preference Theory **c)** a and b **d)** Loanable Funds Theory.
16) The agency estimating the National Income of India is:
a) Reserve Bank of India **b)** Planning Commission **c)** Ministry of Finance **d)** Central Statistical Organisation
17) The goals of monetary policy do not include **a)** Maximum output **b)** Full ernploymeot
c) Price stability ,**d)** Maximum tax revenue
18) Gross National Product (GNP) is: **a)** The total output of goods and services produced by the country's economy **b)** The total domestic and foreign output claimed by residents of the country **c)** The sum of gross domestic product and investment **d)** National income minus national expenditure
19) If an economy is in equilibrium at the point where plans to save and to invest are equal, then government expenditure must be: **a)** Curtailed **b)** Equal to government income **c)** Increased **d)** None of the above
20) Which of the following is correct regarding the gross domestic savings in India?
a) Contribution of corporate sector is largest **b)** Contribution of government sector is the largest **c)** Contribution of household sector is the largest **d)** None of these
21) NNP (Net National Product) or National Income is the money value of
a) Final goods and services produced annually in the economy **b)** Annual service generation in the Economy
c) Tangible goods produced annually in the economy **d)** Tangible goods available in the economy
22) Which of the following is included in the calculation of gross domestic product? **a)** Personal consumption expenditure **b)** Gross domestic investment **c)** Purchase by the government **d)** All of the above
23) Gross National Product is greater than gross domestic product when: **a)** NFI (from abroa**d)** > 0 **b)** NFI < 0 **c)** NFI = 0 **d)** NFI = -1
24) Which of the following is deducted from gross national product in order to estimate net national product?
a) Depreciation **b)** compensation of employees **c)** expenditure on buildings **d)** expenditure on raw material
25) Changes in the standard of living in a country are best reflected in changes in the: **a)** Social Welfare **b)** Economic Welfare **c)** Per capita income at rent prices **d)** Per capital income at constant prices
26) Whicl: is the primary indicator to recognise a country's rate of economic growth? **a)** Increase inter per capita income **b)** Setting of more industries **c)** Rate of growth in national income More exports
27) NationalIncome is based on: **a)** Total Production x prices **b)** Rent + wages + Interest,+ Profit **c)** Domestic Income + NFI **d)** The sum of all factor incomes **e)** All the above
28) Net National Production excludes:
a) Gross Investment **b)** Netinvestment **c)** Foreign Investment **d)** Replacement investment
29) Here are four statements about various national income / expenditure I product relationships. Which one of the following is true: **a)** GNP less NIT = NNP **b)** GNP less NFI = NNP **c)** GNPplus depreciation = NNP **d)** GNP less depreciation allowances = NNP
30) The term GDP incorporates the economic activity: **a)** Taking place within the geographical boundary of the country **b)** Within the land territorial **c)**Within water territorial **d)** Within air space
31) The term "Hindu rate of growth" refers to the 3.5% per annum growth rate achieved by the Indian economy over the first six Five-Year Plans. The term was coined by **a)** Chakravaty **b)** J.N. Bhagwati **c)** Raj Krishna **d)** K.N. Raj
32) Essential services owned and controlled by government is called:
a) Public monopoly **b)** Public utility **c)** Public Sector **d)** All of the above
33) Which of the following is not a fiscal monopoly?
a) Printing of currency **b)** Minting of coins **c)** Electricity supply **d)** None of the above

34) In a planned economy the economic problem of what shall be produced is determined primarily by:
a) Computers deciding what consumers want. b) Direction by the oovernment. c) The pattern of consumer's spending d) The independent decisions of entrepreneurs.
35) Development means economic growth plus: a) Price stability b) Social change c) Inflation d) Deflation
36) Which Plan recommended Zero-Based Budgeting (ZBB) as a step to control public expenditure?
a) Fifth Plan b) Sixth Plan c) Seventh Plan d) Eighth plan
37) All revenues received, loans raised and money received in repayment of loans by the Union Government go into. a) Public Account of India b) Contingency Fund in India c) Consolidated fund in India d) none of the above
38) Which one of the following is not directly the concern of the economist? .a) Choices relating to location of a steel plant b) Bargaining between the workers' unions and the employers c) Effects of a change in money supply. d) Imposition of tax to discourage cigarette smoking
39) Customs duties, export duties, corporation taxes, taxes on capital value of assets (excluding agricultural land of individuals and companies) ate: a) Taxes and duties levied by the Centre but wholly appropriated by the States b) Taxes and duties levied by the Centre but collected by the States c) Taxes and duties that accrue wholly to the Union Government d) Taxes levied and collected by the Union but which are shared with the States.
40) "Funded debt" means: a) All Government securities which are marketable on the stock exchange market b) All private securities c) Shares of Companies d) KisanVikasPatras
41) "Annual Financial Statement" is another name of:
a) Balance of payment b) Fiscal Budget, c) Budgetd) Debt & Credit
42) "Multi-Currency Basket" means: a) Relationship with world bank b) Currency + coins c) Number of major international currencies to which the external value of the Indian rupee is linked d) None of the above
43) Which of the following is not a seiective credit control measure?
a) Rationalizing of Credit b) Open market observations c) Changes in the statutory liquidity ratio d) a and -c
44) Public finance is said to be: a) Science of taxes and pending b) Science of demand and supply of money c) Science of money and cost d) Science of income and expenditure

45) One of the distinctions between public finance and private finance is that:
a) The State adjusts "income to expenditure' while an individual adjusts "expenditure to income" b) The State maximizes the general welfare of the public while an individual maximizes his own satisfaction c) The State has no coercive powers while the individual has d) The State cannot borrow money while the individual can get loans
46) A tax takes away a higher proportion of one's income rise is termed is:
a) Proportional Tax b) Indirect Tax c) Regressive Tax d) Progressive Tax
47 Co orate tax is imposed by:
a) Local Government b) Central Government c) State Government d) Both Central and State Government
48) Which of the following are direct taxes? a) Gift tax b) Income tax c) Corporation tax d) All of the above
49) From the following, which is not a direct tax?
a) Tax on wealth b) Tax on entertainment c) Tax income d) Tax on expenditure
50) An Direct tax is one where: a) Tax is levied always on property b) Points of impact and incidence are different c) Tax is levied on wealth d) Points of impact and incidence are the same
51) The name of Indirect tax is: a) Income tax b) Sale tax c) Corporate tax d) Wealth tax
52) A regressive tax will tend to redistribute income more: a) Equally b) Equitably c) Unequally d) Inequitably
53) Which of the following does not grant any tax rebate?
a) Indira VikasPatra b) Public Provident Fund c) National Saving Scheme d) National SavingCertificate
54) The Indian Income tax is:
a) Direct and progressive b) Obssessive c) Indirect and proportional d) Direct and proportional
55) Temporary tax levied to obtain additional revenue is called: a) Fee b) Surcharge c) Cess d) Rate
56) Which of the following taxes is/are levied by the Central Govt. and collected appropriated by the States?
a) Estate Duty b) Stamp Duties c) Passenger and goods tax d) Taxes on Newspaper
57) Taxes raised are credited into:
a) Consolidated Fund b) Public Accounts c) Contingency Accounts ,d) Private Accounts
58) Generally tax on production are: a) Indirect taxes b) Both A and B c) Direct taxes d) None of the above
59) Tax on incomes is: a) Indirect b) Both A and B c) Direct d) None of the above
60) Which of the following taxes is levied on services?
a) Personal tax b) Value added tax c) Capital gains tax d) Corporate tax
61) Income tax is raised by:a) Local Government b) Central Government c) Municipality d) State Government
62) Sales tax is levied by: a) Local government b) State government c) Central government d) None of the above
63) Union Excise Duties are a part of Central Government's:

a) Tax revenue **b)** Capital receipts **c)** Non-tax revenue **d)** None of the above
64) All taxes come under: **a)** Capital receipts **b)** Revenue receipts **c)** Public debt **d)** Both A and C
65) In India, the States gets maximum income from:
a) Sales tax **b)** State Excise duties **c)** Land Revenue **d)** Agricultural Income tax
66) Progressive tax in India is: **a)** Income tax **b)** Wealth tax **c)** Corporate tax **d)** Sales tax
67) Which of the following is a direct tax? **a)** Sales tax **b)** Entertainment tax **c)** Excise duty **d)** Estate duty
68) Which of the most important source of revenue to the State Government of India ?
a) Land Revenue **b)** Agriculture Income-tax **c)** State excise duties **d)** Sales tax
69) A budget is the summary of:
a) Proper allocation of resources **b)** Income reallocation **c)** Resource reallocation **d)** Revenue and expenditure
70) The budget deficit refers to the difference between all-revenue and expenditure of:
a) Revenue account only **b)** Increased government expenditure **c)** Capital account only **d)** Both revenue and capital accounts
71) Borrowing from capital market is a part of: **a)** Revenue budget **b)** Capital budget **c)** Both a and b **d)** None of these
72) Revenue deficit in India is: **a)** Negative **b)** Positive **c)** Zero **d)** None of 'he above
73) Capital deficit in India is: **a)** Positive **b)** Zero **c)** Negative **d)** None of the above
74) Funds, which do not belong to the government, are?
a) Consolidated fund **b)** Contingency fund **c)** Public accounts **d)** None of the above
75) Which budget in India is passed separately? **a)** Airlines **b)** Railways **c)** Defence **d)** Atomic energy
76) Which one of the following cannot be influenced by budgetary policy? **a)** Power of private monopolies **b)** Balance of trade **c)** General level of prices **d)** Regional distribution of employment
77) Which budget is measured in financial terms only?
a) Dominance budget **b)** Programme performance budget **c)** Zero-base budget **d)** Central budget
78) Deficit Financing means: **a)** Government spends in excess of revenue and capital receipt to that budget deficit in incurred which is financed by borrowing from the RBI. b) Difference of total expenditure & income revenue from all sources. **c)** Difference in borrowing an internal and external resources **d)** Capital expenditure on items of public construction, public enterprises and public borrowings.
79) The need for deficit financing in India arises due:
a) Failure of the government to mobilize the desired volume of surplus for the public sector plans. **b)** The rapidly growing expenditure incurred by the government **c)** Neither A nor B. ' **d)** Both A and B
80) Deficit financing leads to: **a)** Inflation **b)** Capital formation **c)** Neither A nor B ?**d)** Both A and B
81) Deficit financing means: **a)** Difference in borrowing and internal and external resources **b)** Capital expenditure on items of public construction, public enterprises and public borrowings **c)** Government spends in excess of revenue and capital receipts so that budget deficit is incurred which is financed by borrowing from the RBI. **d)** Difference of total expenditure and income by revenue from all sources
82) The effect of deficit financing is: **a)** Never inflationary **b)** Always inflationary **c)** Sometimes inflationary and sometimes not so depending cn conditions of the economy and the dose of deficit financing.**d)** None of these
83) The direct effect of deficit financing is:
a) Deficit financing leads to extra money supply which in turn pushes up prices **b)** Demand and supply both increase **c)** The price situation comes under complete control dj Deficit financing leads to extra money supply, which in turn makes market more & more competitive.
84) Fiscal policy is related to: **a)** Exports and Imports **b)** Public revenue and expenditure **c)** Issues and circulation of currencies **d)** Monetary Control measures
85) A restrictive monetary-fiscal policy is a good way to deal with:
a) Demand— shift inflation **b)** Any short of inflation that occurs when the economy falls below full employment **c)** Demand — pull inflation **d)** Cost — push inflation
86) Grants—in-aid given by the Centre to the states is meant: **a)** To cover the gaps on revenue accounts. **b)** For flood control **c)** Po(boosting agriculture in the State. **d)** For financing State plan projects
87) The finance commission is appointed every: **a)** 7 years **b)** 6 years 'C) 5 years **d)** 3 years
88) The Narsimham Committee submitted its report to the government on:
a) Depoliticising appointments in public sector undertakes b) Import and Export c) NPA **d)** Banking structure
89) "Interest is the reward for pure waiting." Which theory of interest explains it? **a)**Time Preference Theory **b)** Classical Theory **c)** Liquidity Preference Theory **d)** Loanable Funds Theory
90) What is not true for the Classical theory of interest? **a)** Demand and Supply Theory **b)** Saving-Investment Theory **c)** Non-monetary Theory **d)** Monetary Theory of Interest
91) The Loanable Funds Theory of interest is also known as: **a)** The neo-classical theory of interest **b)** The classical

theory of interest **c)** The real theory of interest **d)** The modern theory of interest

92) Rate of interest is a function of I, S, M, r = f (I, S, M, L) is explained by which of the following theories?
a)Liquidity Preference Theory **b)** Saving-Investment Theory **c)** Loanable Funds Theory **d)** Modern Theory

93) For which of the following motives for liquidity preference, the demand for liquidity is determined by the rate of interest? **a)** Transaction motive **b)** Precautionary motive **c)** Speculative motive **d)** All the three motives.

94) Which of the following is known as monetary theory of interest?
a) Loanable Funds Theory **b)** Modern Theory **c)** Liquidity Pi eference Theory **d)** Saving-Investment Theory

95) What is not true of the modern theory of interest?
a) Neo-Keynesian Theory **b)** Hicks and Hansen's synthesis **c)** Monetary Theory **d)** IS-LM Curves Analysis

96) Which of the following is not a c4Idracteristic of business cycles?
a) Recurrent in nature **b)** Periodicity **c)** Regular **d)** Cumulative

97) Who gave innovation theory of business cycles ? **a)** Pigou **b)** .1. A. Hobson **c)** Schumpeter **d)** J. Tinbergen

98) Which of the following assumptions is not correct in relation to Hicks' theory of business cycle ?
a) The equilibrium of the economy is influenced by changes in consumption and investment **b)** Fall employment is the ceiling of expansion **c)** Autonomous investment increases at some constant rate even during depression **d)** Accelerator remains operative in all phases of business cycle, but the multiplier stops operating during depression

99) Economic growth refers to :
a) An increase in per capita income at current prices **b)** A sustained increase in per capita output **c)** An increase in income and output in real terms and not in money **d)** An increase in economic welfare

100) National income differs from NNP at market prices by the amount of : **a)** Current transfers from the rest of the world, **b)** Net indirect taxes .9-) National debt interest, **d)** It does not differ

ANSWER

1	A	2	C	3	A	4	D	5	A	6	B	7	A	8	B	9	B	10	C
11	C	12	C	13	D	14	A	15	D	16	D	17	D	18	B	19	B	20	C
21	A	22	D	23	A	24	A	25	D	26	C	27	E	28	D	29	D	30	A
31	C	32	D	33	C	34	B	35	B	36	C	37	C	38	A	39	C	40	A
41	C	42	C	43	D	44	D	45	A	46	D	47	B	48	D	49	B	50	B
51	B	52	C	53	A	54	A	55	B	56	A	57	A	58	C	59	C	60	B
61	B	62	B	63	A	64	B	65	A	66	A	67	D	68	D	69	D	70	D
71	B	72	A	73	A	74	C	75	B	76	A	77	B	78	A	79	D	80	D
81	C	82	C	83	A	84	B	85	B	86	A	87	C	88	D	89	B	90	D
91	A	92	C	93	C	94	C	95	C	96	C	97	C	98	D	99	B	100	B

Module: B

Business Mathematics

SYLLABUS

Concept of time Value of Money - Net Present Value - Discounted Cash Flow - Sampling methods - presentation of data - analysis and interpretation of sample data - hypothesis testing - Time series analysis - mean / standard deviation - co-relation - Regression - covariance and volatility - Probability distribution - Confidence interval analysis - estimating parameters of distribution - Bond valuation - duration - modified duration. Linear programming - decision making-simulation - Statistical analysis using spreadsheets. Features of Spread sheet - Macros, pivot table, statistical and mathematical formulae.

TIME VALUE OF MONEY & PRESENT VALUE

Cash flows at different time intervals : When cash flows take place at different time intervals, their value is different fora ·no. of reasons such as interest factor, inflation, uncertainty etc. In order to ascertain their value, these flows are required to be compared. The comparison is possible by using a time line that shows the value and tuning of cash flows. " ' - ;

Positive cash flow:When a firm receives cash which is called inflow, it is positive cash flow.

Negative cash flow :When a firm makes payments, this is outflow of cash and is called negative cash flow.

Future cash flow Si present cash flow .

Future cash flows are worth less than the present cash flow.Rs.100 available with a person presently And Rs.100to be received after a year, carry higher present value. It is because, the people prefer consumption presently rather than in future and to put off their consumption for future, more value requires to be offered. Similarly due to inflation, there is erosion in money value. Further there is uncertainty about receipt of money in future. ,

Discount rate ; Discount rate is 'a process by which the future cash inflows are adjusted/discounted - atc.ording the their present value. (say Rs.100 received at the end of a year, if discounted at say 10%, will give a value around Rs.90).

Trade-off' : When present consumption is put-off; for some future time period in return for some monetary return such as interest, this is called exchange or Trade Off.

Different kinds of cash flows

Cash flows can be simple cash flows, annuities, growing annuities, perpetuities and growing perpetuities. Simple cash flow.

It is single cash flow to occur at a specified future time. Say Rs.1000 to be received at the and 'of one-year. Its present value can be worked out by discounting hack by using an appropriate discount rate.

Calculation of present value :

The present value can be calculated by using the formula

PV = Discount Factor x CI OR PV = 1 (l+r) x Cl *(where CI is the expected cash flaw at the end olperiod I)*

Example : A person wants to get Rs.10 lac after one year. With prevailing interest rate of 9%; how much he should invest.

= 10;00,000 / 1.09 = 917531.19 Calculation of net present value

It can be calculated as NPV= PV-required investment OR it can be calculated as = Co + (Ct / **(11-r)**

Co = Cash flow at time 0 le. today. `r·' means rate of discount.

Example : You proposes to invest Rs.8 lac in a house and expect that it will fetch Rs. l0 lac at the end of the year. At 9% interest rate, what is the net present value. Use the data in the above problem.

PV-required investment = 917531.19 --·800000 =117531.19

Effect of inflation on the discount rate.

The inflation reduces the purchasing power of future cash flows and it reduces the value of future cash flows.

Conversion of the nominal cash flows at' future period to real cash flows.

Real cash flow ^{w} (Nominal cash flow) / (1+ inflation rate)

If the inflation rate is 10% per annum and an investor expects Rs.10 lac, what will be his real cash flow.

Real cash flow = (Nominal cash flow) / (1+ inflation rate)

= 10,00,0001 1+10% = 10 lac / 1.10 = Rs. 909091

Risk and discount rate: Higher the risk due to uncertainty, higher would be discount rate used to

calculate the present value of the cash flow.

Importance of discounting of the cash flows.

The comparison becomes easier for cash inflows of different periods.

The user becomes indifferent for present and future cash inflows and can take more rationale decisions.

Future value of a present cash flow:

This can be done by way of compounding by using the formula

CF 0 (1+0' *where (` = at the end of period) (CF 0 = present cash flow) and (r = rate of discount)*

Rule of 72:

This is the approximate answer to find out as to in how much period the amount will become double at a particular interest rate. if 72 is divided by the interest rate, the resultant product, is the time period during which the amount will be doubled. For example if the interest rate is 8%, the amount will double in 9 years.

Effective rate of interest.

It is the actual rate of interest that takes into account the compounding effect of interim interest payment, if any.

Determination of effective rate of interest

It can be done by using the following formula:

(I+ given annual RoI)" I N - I (where N = no. of compounding periods. Say 12= months).

Where the annual interest rate is 20%, what will be effective rate, where the compounding is on half-yearly (semi-annual) basis.

(1+ given annual RoI)" /N - 1

$(110^{2}$ - I)= 1.21-1.00=21%

Continuous compounding & calculation of effective interest rate :

It can be computed as = exp ^{r} - 1 (where 'exp' means exponential function and `r·' means given interest rate.

Effective rates for various compounding frequencies for 10% RoI:

Where compounding frequency is annual. : Effective RoI = 0.10 = 10%

Where the compounding frequency is semi annual: Effective RoI = (1 + 10/2) ^{2} - 1) = 10.25%

Where the compounding frequency is monthly : Effective RoI = (1 + 10/12) ^{12} - 1) = 10.47%

Where the compounding frequency is daily : Effective RoI = $(1 + 101365)^{365}$ - 1) = 10.5156%

Where the Compounding frequency is on continuous basis: Effective RoI = e.$^{i°}$ - 1) = 10.5171%

More frequent compounding & effective rate :

Effective rate increases and present value of future cash flows decreases. Annuity.

It is a constant cash flow occurring at regular intervals of time at fixed period of time.

It can occur at the beginning of each period or at the end of each period.

Present value of an end-of-the period annuity :

= PV·(A,r,n) = A f I-(1/ $(I+r)^{n}$ /r

(A = annuity r=discount rate n=no. of years.

Calculate the PV of Rs:9000 each year for 5 years where RoI is 12%.= PV (A,r,n) = A {1-(1/ $(I+r)^{n}$ = 9000 $\{I-(1/ (1+12)^{5}$). / 0.12 = 32442.98

Future value of an end-of-the period annuity : FV

(A,r,n) = A {(1 $^{4",-)^{11}}$- I } r

(A = annuity r=discount rate n=no. of years.

Calculation of Annuity given future value : =

A(FV,r,n) = FV r / (I+r) -

Baloon repayment loan

It is a loan in which repayment of interest only is made during life period of the loan. The amount of loan is repaid in one instalment at the end of repayment period, such as debentures and bonds. The companies

raising bonds or debentures set aside funds in a sinking funds maturing with maturity period of the loan, so that do not face, any problem at the time of repayment.

Sinking fund

It is fund created by companies for meeting special repayment obligations in which regular contributions are made on annual or other basis.

Present value of annuity beginning-of-a-period over n years :

=A-FA (I-(1/(1¯1-r)$^{n-1}$ /r

Present value of a growing annuity :

=A (l+g){(1 -(I +g)" / (l+r) ^{n}) / (r g) (g stands for expected growth rate)

Present value of a growing annuity for n years be calculated when r = g

It is = nA

Perpetuity

It is a constant cash flow paid or received at regular time intervals forever. such as a life time pension or rentals received from use of land.

Calculation **of present value of perpetuity :**

It can be calculated by use of the formula : A *i* r

Console Bond.

It is a bond which does not have maturity. On such bond fixed coupon of Rol is paid.

An investor has a console bond of Rs.I0000 with 8% fixed coupon. lithe interest rate is I0%. the current value of the bond would be:

= A t.r = 80/0.1 = 8000

When the COUD017 rate is equal to interest rate, the value will be equal to face value.

Growing perpetuity_

It is a cash flow which forever, is expected to grow at a constant rate.

The present value of a ;rowing perpetuity can be written as.. CI I (r-g)

BOND VALUATION

Loans can be raised by the Govt. and corporations in the form of Bonds. *Bonds are the instrument of borrowing with fixed maturity, fixed value at maturity and interest payment. These are redeemed at par. In* return, the Govt. makes promise to return a specific amount to the bond holders (who are lenders).

Regular payment on the bonds in the form of interest on bonds is called coupon. On maturity the bond holder receives the face value 'of the bond.

Let us take an example that a 6% bond is issued by RBI with a face value of Rs-1000 with a maturity period of 3 years. Investor here gets Rs. 1 000 on maturity in addition to annual payment of Rs.60 being the coupon.

Different kinds of bonds

Convertible bonds : These bonds can be converted into shares at a specified rate and time period. Such bonds provide an opportunity to the investor to participate in equity.

Callable bonds : When the issuer reserves the right to call back the bond and pay a fixed price (may be with premium). Since interest yield declines in such bonds, these are less attractive.

Floating rate bonds : When the interest rate can be changed over a time period and yield is linked to current market rate by reset of the interest rate. This ensures that the yield on the bonds is near the current market returns.

Negative bonds : These bonds are traded in the market and their face value changes depending on the current interest rates.

Zero coupon bonds: These bonds are priced at a nominal value *below their face value-and* are redeemed at their face value. The investor gets return as difference between the purchase price and face value.

Other terms

Coupon rate : It is interest rate specified in the bond and the fixed income is dependent on this rate.

Yield to maturity.: it is the discount rate which makes the present value of the bond's payment equal to its price. It is a measure of the average rate of return an investor earns over the bond's fife, if it is held till maturity.

Current yield : It is the current return and does not take into account the bond price fluctuations.

Effective yield : Actual yield (instead of the nominal amount) compared to the market situation. It can be less or more than the current yield.

Price risk : The risk arising on account of fluctuation in the bond prices, that effects the return.

Rate of return : It is calculated for any particular holding period and is based on the actual income and the capital gain or loss on the bond over that period.

Bonds prices and yields

In certain cases, these bonds are listed on stock exchange, where trading takes place, in these bonds. Bond prices are normally quoted as %age of their face value. As the interest in the above example (opening paragraph) shall be received on yearly basis and Rs.I000 will be available after 3 years, the present value of cash flow has to be worked out. It is presumed that the prevailing interest rate on 3-year maturity offers a *compounded return* of 5,6%. Present value would be:

$PV = \frac{Rs.60}{(1\text{-}Er)^{2'}} + \frac{Rs.60}{'(1+r)^{3}} + \frac{Rs.1060}{}$ *r* compounded rate

$PV = \frac{Rs.60}{(1.056)} \quad \frac{Rs.60}{(1.056)^2} \quad \frac{Rs.1060}{(1.056)^3}$ PV = Rs.1010.77

Hence the 6% bonds is worth 101.077 % of the face value. Its price would be quoted around this amount.

Value calculation.on the basis of annuity formula:

The value can be calculated on the basis of annuity formula as Rs.60 which are received every year for 3 years. PV = PV of Coupons 1- PV of face value

$= 60 \left(\frac{I/}{(0.056)} - \frac{1}{0.056(1.056)'^{3}} \right)$ = 161.57 + 84920 = 1010.77

Bond prices with half-yearly coupon

In the above case, the coupon payment was yearly. But if the payment is on a half yearly basis, the compounded return would be halved i.e. 5.6 / 2 = 2.8%. In this case the value would be Rs.I010.91 as calculated as under:

$PV = \frac{Rs.30}{(1.028)} + \frac{Rs.30}{(1.028)^2} + \frac{Rs.30}{(1.028)^3} + Rs.30 \left(\frac{1}{(I.028)^4} + \frac{1}{(1.028)^5} + \frac{1}{(I.028)} \right) + \frac{Rs.1030}{}$

PV = Rs.I010.91

It will be observed that with reduction in compounding intervals (say from annual to half-yearly), the yield
increases.

Bond prices and varying interest rates

With change in interest rates, bond prices change.

The price can be worked out if the discount rate is 6%

$PV \text{ at } 6\% = \frac{Rs.60}{(1.06)} + \frac{Rs.60}{(1.06)^2} + \frac{Rs.1060}{(1.06)^3}$ PV = Rs.1000.00

It means that if interest rate is same as the coupon rate, the bond sells for face value.

If the interest rate change from 6% to say, 15%, the bond price would be Rs.794.5 I as under: $PV \text{ at } 15\% = \frac{Rs.60}{(1.15)} + \frac{Rs.00}{(1.15)^2} + \frac{Rs.1060}{(1.15)^3}$ PV = R.s.794.51 Hence this bond can sell at Rs.79.45.

It may be remembered that:

- whenever the market interest rate exceeds the coupon rate, the bonds for less than the face

value and

- when the coupon is more than the current market, the bonds earn premium.

Yield to maturity and current yield

The current yield on a bond could be less than or more than the yield to maturity. For instance,, if a bond is issued for face value Rs. I 000 for 3 years at 10% coupon, its return would be Rs.100 at the end of 2nd year and 3"I year. In the 3"I year the face value will also be received by the bond hold. Hence-the return is 10%.

Now let *us* assume that some one else purchases this bond for R5.1136.16. The return on this investment shall not be 10% because this time the return of Rs.100 will be available for an investment of Rs.1136.16. It shall be:

100 / 1136.16 x 100 = 8.8% . This is current yield.

Yield to maturity

The total yield on a bond would depend on the capital gains or losses over the time period of the bond. Investors who purchase bonds at premium, have to face capital loss and those who are able to buy it at a discount, earn capital gains. The measure thayakes into account both the current yield and the change in a bond value over its life period, is called *yieldlo maturity.*

In the above example the yield to maturity is only 5% as the PV at 5% coupon is Rs.1136.16, as under:

$$\text{PV at 5\%} = \frac{\text{Rs.100}}{(1.05)} + \frac{\text{Rs.100}}{(1.05)^2} + \frac{\text{Rs.I 100}}{(1.05)^3} \qquad \text{FEW= Rs.1136.16}$$

Rate of return

An investor purchase of 6% bond with a 3 year for Rs.'1010.77. He sells it for Rs.1020 next year. The return of this investor is not only Rs.60 being interest he has earned but also the difference in price at which purchased and sold (i..e. capital gains in this case) of Rs.9.33 (1020 -1010.77).

Rate of return = (coupon income + price change)/ investment

Rate of return = (60 + 9.33)/ 1010.77 = 0.686 or 6.86%

Rate of return and yield to maturity

An investors invests Rs.] 010.77 *in* a bond to mature in 2007, with 3 years left until maturity. It YTM is 5.6%. Suppose. by the end of the year, the market interest rates have fallen to 4%, the value of the bond (after one year) would be Rs.1037.72 as under:

$$\text{PV at 4\%} = \frac{\text{Rs.60}}{(1.04)} + \frac{\text{Rs.1060}}{(1.04)^2} \qquad \text{PV = Rs. I 037.72}$$

The investor gets Rs.60 + 26.95 (1037.72 - 1010.77) = 86.95.

His rate of return would be: 86.95 / 101037 = 8.6%

.. The YTM in the beginning of the year was 5.6% but due to fall in interest rate, the rate of return increased to 8.6%.

It can also be concluded that :

- If the bond's yield to maturity remains unchanged during an investment period, its rate of return will be equal to that yield.

-if the bond's yield to maturity increases during an investment period, its rate of return will be less than YTM.

-if the bond's yield to maturity decreases during an investment period, its rate of return will be more than YTM. **Interest rate risk**

The YTM of bond fluctuate with the interest rate movement due to which the bond investment carries interest rate movement risk. With market interest rate falling, the investors of bonds, gain. On the other hand with increase in current market interest rates, the investor are bound to lose.

MCQ ON TIME VALUE OF MONEY

1 Money has a time value is shown by which of the following concepts:

a: market value
b: face value
c: present value
d: b and c

2 The cash inflow is called:
a: negative cash flow
b: positive cash flow
c: balanced cash flow
d: b or c
3 The cash outflow is known as :
a: negative cash flow
b: positive cash flow
c: baked cash flow
d: a''CF:c
4 A e ash flow of future has less value due to which of the following (which is not correct):
a: prgent consumption is preferred over future consumption
b: money value gets eroded due to inflation
c: receipt of cash in future is subject to uncertainties
d: none of the above
5 The process through which the future cash flows are adjusted is called:
a: discointing
b: compounding
c: balancing
d: any of the above •
6 The rate at which the present and future cash flows are traded off (exchanged), is called:
a: interest. rate
b: discount rate
c: compounding rate
d: yield to maturity
7 If inflation rate is higher in an economy, the discount rate should generally:
a: be Cower
b: be higher
c: be stable cl: be fluctuating
8 If there is lower level of uncertainty about future cash flows, the discount rate should generally:
a: be lower
b: be higher lc: be stable
d: be fluctuating.
9 A lower discount rate leads to __present value for the future'rash flcv;s:
a: stable
b: higher *lc:* lower ,
d: fluctuating
10 Cash flows of different points of time can be compared or aggregated by:
a: converting them to future flows
b: brining them to the same point in time
c: converting them to standard flows
d: a or b
11 Which of the following is not a type of cash flow:
a: simple.cash flow
b: annuities or growing annuities
c: perpetuities or growing perpetuities
d: future yields to maturities
12 A single cash flow in a specified future time period is called:
a: simple cash flow
b: annuities
c: perpetuities
d: growing annuities

13 The process in which a present cash fowls converted in to its expected future value is called:
a: discounting
b: .compounding c balancing d: any of the above

14 Present value can be calculated as .=x C 1, where C i means the expected payoff at period 1
a: Compounding factor
b: discount factor
c: interest factor
d: yield factor

15 Value today of Re 1 to be received in future is called:
a: present value
b: compound factor
e: discount factor , d: - yield factor

16 Discount factor is denoted by which of the following:
a: 1 / (1-r)
b: 1 / (1-1-r)
c: 1 x (1-r)
d: 1 x

17 X is-expecting a cash flow of Rs.10 lac at the end of one year. At 8% discount rate, what is the present value:
a: 952692
b: 962592
c: 925926
d: 925962

18 Present value - required investment = ?
a: discounted value
b: compounded value
c: net present value
d: future value

19 X is expecting a cash flow of Rs.1.0 lac at the end of one year for his investment of- Rs.8 lac in a housing property. At 8% discount rate, what is the net present value:
a: 152692
b: 125926
c: 162592
d: 125962

20 C 0/ {C i / (11-0} (where C o represents cash flow at time 0 i.e. today -and C1 at the end of one year), stands for:
a: present value
b: net present value
c: future value
discounted value

21 Real Lash flow = _____ / (1 + inflation rate)
a: actual cash flow
b: nominal cash flow
c: present cash flow
d: future cash flow

22 Z decides to invest Rs.9 lac in an iiarnovab!e property that fetches him Rs.5 lac, at the end of an year, what is his return (use.the formula profit investment):
a: 10%
b: 15%
c: 20% • cl:
25%

23 An investment opportunity cart be availed tvhere the net-present value is
a: zero b.negative

c: positive
d: none of the abOve

24 An investment opportunity can be avaifed.where the rate of return is their_____cost of capital:
-a: tessthan, discount
b: more than, opportunity cost
c: less-than, opportunity cost
d: more than, discount

25 Future value of a simple cash flow = x (t+r) ^{t} where r is discount rate:
a: future cash flow called CF
b: present 'cash flow called CF 0
c: discounted cash flow called CF 0
d: none !·f the above

26 With the help of formula (1 + stated annual interest rate) .^{n}/ N) - 1.(where N stands-for no. of compounding periods say semi annual -^{4}-2-and monthly = 12) which of the following can-be calculated:
a: -discounted value *.
b: nominal interest rate
c: effective interest rate .
d: yield to maturity .

27 The rate of interest is 8% and compounding is semi-annual,- what will be effective-interest rate: • a: 8%
b: .8.16%
c: 8.25%
d: 8.32%

28 If the rate of interest is 10% and compounding is annual, what will be the effective interest rate: a: • 10%
10.25%
c: 10.47%
d: 10.5171

29 If the rate of interest is 10% and compounding is semi-annual, what will be the effective interest rate:
a: 10% b: 10.25%
c: 10.17% d: . 10.5171

30 If the rate of interest is 10% and compounding is monthly, what will be the effective interest rate:
a: 10% b: 10.25%
c: 10.17% 4: 10.5171

31 If the rate of interest is 10% and compounding is continuous, what will be the effective interest rate:
a:.. 10% b: 10.25%
c:$_{o}$ 10.97% d: 10.5171

32 A continuous cash flow that occurs at regular interval of time is called:
future value b: present value
c: perpetuity d: annuity

33 Present value of annuity can be calculated by use of which of the formula: (where A = annuity, r=discount rate n = no. of years, g= expected growth rate
a: PV (A, g,n) b: PV (A, r,n)
c: PV (A, r,g) d: PV (g, r,n)

34 What is the present value of Rs.180000 which is paid every year over a period of 5 years by assuming the rate of interest at 12%:
a: .398680
b: 346880 '
c: 348860
d: 381860

35 Future value of an end-of-the-period annuity can be calculated as:
a: FV (A, r, g)

b: FV (A, g, n) C: FV
(A, g, r)
d: FV (A, r, n)

36 A loan for which only interest is paid during its repayment period while the principal is repaid at the end is called:

a: term loan
b: interest demand loan
c: lump-sum payment loans .

balloon repayment tioan

37 Which of the following is an example of a balloon repayment loan:

a: bonds and debentures
b: bonds and term loans
c: debentires and term loans
d: all the above

38 A fund which *is* created by companies to make payment of balloon repayment loans by regular annual contributions to have adequate funds at the end of the period, when repayment falls due is called:

a: reserve fund
b: balloon fund -
c: sinking fund
d: repayment fund

39 A cash flow that grows at a constant rate for a specified period of time is called:

a: annuity
b: perpetuity
c: growing annuity
d: growing perpetuity

40. Present value of a growing annuity for *n* years can be calculated, where r=g:

a: growing annuity x no. of periods over which cash flows-are to be received or paid
b: annuity x no. of periods over which cash flows are to be received or paid
c: growing perpetuity x no. of periods over which cash flows are to be received or paid
d: none of the above.

41 A constant flow paid orseceived at Tegular time intervals for ever is known as:

a: annuity
b: perpetuity
c: growing annuity
d: growing perpetuity

42 A bond that has no maturity and pays a fixed coupon (or rate of interest) is called:

a: long term bonds
b: perpetual bonds

c: console bonds
d: non-repayable bonds

43 A cash flow that is expected to grow at a constant rate forever, is called:

a: annuity
b: perpetuity
c: growing annuity
d: growing perpetuity

Answers

01	c	02	b	03	a	04	d	05	a
06	b	07	b	08	a	09	c	10	b
11	d	12	a	13	b	14	b	15	c
16	b	17	c	18	c	19	b	20	b
21	b	22	d	23	c	24	b	25	b
26	c	27	b	28	a	79	b	30	

31 d 32 cf 33 b 34 c 35 d
36 d 37 a 38 c 39 c 40 a
41 b 42 c 43 d

BOND VALUATION

Bonds have a ıaturity and value at
fixed, variable ıaturity:
fixed, fixed
variable. fixed

2 Regular repayment in the form of interest on a bond is called:
a: discount
b: interest
c: coupon
d: dividend

3 On 8%, 5 year bond of Rs.10000, the investors gets_____ annually, as
a: 80.00, interest
b: 800.00, discount
c: 80.00, coupon
d: 800.00, coupon

A bond the value of which is changed into a share is called:
a: convertible bond '
b: zero coupon bond
c: negative bond
d: floating rate bond

5 A bond where the interest rate can be reset is: a: convertible bond,b zero coupon bond
c: negative bond,
d: floating rate bond

6 Abond is issued at a price below its face value while on payment, the face value is paid:
a: convertible bond
b: zero coupon bond
c: negative bond .
d: floating rate bond

7 In which of the following bonds, no interest payment is made:
a: convertible bond •
b: zero coupon bond
c: negative bond
d: fldating rate bond

8 The income that a bond earns from year to year is called:
a: coupon
b: yield to maturity
c: current yield
d :effective yield. .

9 The actual yield to an investor, instead of nominal interest, is called:
a: coupon
b: yield to maturity c current yield d: effective yield '

10 The discount rate that makes the present value of bond's payment equal to its price is called:
a: coupon
b: yield to maturity
c: current yield
d: effective yield

11 A risk that arises on account of change in the current market price of the bond, is known as:
a: interest risk
b: yield risk
c: return risk
d: price risk
12 The return to an investor in case of zero coupon bond is different between the-- price and--value:
a: sale, face
b: face, purchase
c: purchase, face
d: face, sale
13 The face value of bond changes with current interest rates:
a: convertible bond
b: zero coupon bond
c: negative bond
d: floating rate bond
14 Coupon / (1+r), where ris compounded return
a: future value
b: discount rate
c: present value
d: maturity value
15 To calculate present value under annuity formula, we use the following:
a: PV of investment + PV of face value
b: PV of coupbri + PV of face value
c: PV of coupon + PV of investment
d: PV of interest + PV of investment
16 For a 3 year 6% bond of R5.1000, the present value is . if the compounding is annual:
a: Rs.1010.77
b: Rs.1010.91
c: Rs.1100.77
d: Rs.1017.11
17 For a 3 year 6% bond of Rs.1000, the present value is , if the compounding is semi-annual (half yearly):
a: Rs.1010.77
b: Rs.l010..91
c: :Rs.1100.77
d: Rs.10l7.11
18 Where the current market interest are lower that the fixed coupon rate of a bond:.
a: bond is sold at a discount to face value
b: bond earns premium on face value
c: hand sells at par
d: there is no effect
19 Where the current market interest rate is higher than the fixed coupon rate of a bond:
a: bond is sold at a discount to face value
b: bond earns prerniirm on face value
c: bond sells at par
d: there is no effect
20 Where the currentinarketrate of interest is equal to coupon rated' the bond:
a: bond is sold-at a discountto face value
b: bond earns prethium on face value
c: bond is traded at par
d: there is no effect

Answers

01 b	02 c	03 d	04 a	05 d
06 b	07 b	08 c	09 d	10 b
11 d	12 c	13 c	14 c	15 b
16 a	17 b	18 b	19 a	20 c

Sampling methods & Data presentation

SAMPLING METHODS / DATA PRESENTATION

Population means an aggregate of items to be studied for an investigation. Population may be finite or infinite. Finite population means limited no. of items say 14 banks, 100 branches. Infinite population means unlimited items bank customers, bank borrowers etc.

Sample on the other hand means that part of the population (or universe) which is selected for the purpose of investigation. The technique of statistical investigation based on sample data is called sample method.

Census and sampling: In census, the information is obtained from all items but in sampling it is done from limited items. Census is suitable where the area of investigation is relatively small. There is greater degree of accuracy in census. On the other hand its cost is very high and cost of sampling is smaller. Verification of information collected under sampling is possible.

Statistics : It is a measure that describes the characteristics of a sample.

Parameter : it is the value that describes the characteristic of a population. Expressing Population & Statistics:

Roman letters in lower case are used for sample statistics and Greek or Capital letter are used to denote population characteristics.

Symbols used for population parameters: Population size = N Population Mean = µPopulation standard deviation :

Symbols used for sample statistics: Sample size = n sample mean = (called X-Bar)

Sample standard deviation = S

VARIOUS SAMPLING METHODS

Selection of samples from population:

Random or probability sampling (where any item has the possibility of being selected) and non-random or Judgment sampling, (where identification is done on personal knowledge or opinion).

Methods of random sampling:

Random sampling, purposive (deliberate) sampling, stratified or mixed sampling, systematic sampling, quota sampling, convenience sampling etc.

Simple random sampling: Where samples are selected by a method that permit each possible sample to have an equal probability of being picked up and each item in the entire population has an equal chance of being included in the sample.

Selection of elements in systematic sampling : These are selected from the population at a uniform level that is measured in time, order or space. -

Purposive (deliberate) sampling: it is the method in which the investigator himself makes the choice of the sample· items that in his opinion are best represent the universe (population). Hence, the items are not left to the chance factor.

Standard or mixed sampling: Under this method, sampling is generally adopted when the population consists of different groups with different characteristics. *Population¯is divided into different parts (strata) having different characteristics and some of the items are selected each strata, to ensure proper representation.

Systematic sampling : As per this method, the units of population are numerically, geographically and· alphabetically* arranged-. Every n^{ib} item of the numbered items is selected as a sample item. If 10 out of 100 students are to be taken, every $10^{11'}$ items would be selected.

Cluster sampling : When population is divided into groups or clusters and selection is made on a random

basis out of these clusters. It can produce a more precise sample at considerably less cost than that of simple random sampling. Those groups which are similar, within a population. Such groups could have wide internal variation.

Judgement sampling : A method for selection of samples from a population where personal knowledge is used to identify the items Tor including in the sample..

Quota sampling : Under this method; the population is divided into different groups..or classes according to different characteristics of the population. Some Percentage of different groups in total population is fixed.

Sampling distribution :of the mean : A probability distribUtion of all the possible means of samples of a given size say n, from the population.

Sampling distribution of a statistics : It is probability distribution of possible means that a. statistic may take,.

Sampling error It.is 'variation (or error) among sample statistics due to chance, between each sample and the population and among. several samples that :are due the seleeted elements only:'

Sampling' fraction: It is the proportion (or fraction) of the population in a sample..

Standard error of The mean: The standard deviation of the Sampling distribution of the mean.

Central Limit Theorem; it is a theory that states that the sampling distribution of-the mean-approaches normality as the sample size increases. ThiS is regardless of the shape of population distribution from which the sample is selected.

Finite population: A population that has a size which is already stated or limited.

Infinite population :A population in whiebit is not-possible to observe all elements

Statistical inference': It is the process of drawing inferences about populations from information available in samples.

Relationship between standard error and sample size : If dispersion decreases i.e. if a X becomes smaller, the value taken by the sample mean tend to cluster more closely around p. On the other hand if the dispersion increases i.e. if a 5:< becomes larger, the value taken-by the sample Mean tend to cluster less closely, around. In other words when the standard error decreases, the value of any 'sample mean will probably be eloser.to the value of the population mean.

BASICS OF STATISTICS

Data : Data are numerical statements of aggregates. For example. the no. of public sector banks in India is 28 and that of private sector banks is say, 30. Data is either primary or secondary.

Primary data is the collection of the data by the investigators themselves,

Secondary data means data already collected or published and obtained by the investigator from those sources_ Data can be obtained from the population (all) or as sample (limited).

Population means an aggregate of all items to be studied for an investigation. Population may be finite or infinite. Finite population means limited no. of items say 14 banks, 100 branches. Infinite population means unlimited items say, bank customers, bank borrowers etc.

Dispersion :Dispersion refers to variation and variation' can be with reference to items among themselves or items around an average. Dispersion is measure of the extent to which the individual 'items vary.' Dispersion can be measured by 'various methods/measures that may come under absolute' Measure (range., quartile deviation, mean deviation, standard deviation etc.) or relative measure (coefficient of range, coefficient of mean deviation, coefficient of standard variation etc.).

Mean deviation : It is the arithmetic average of the deviations of all the values taken from some average value (mean, median, mode) of the series, ignoring the sign's (+ or -).

Standard deviation : it is square root of the arithmetic means of the squares of all-deviations. It can be calculated as {(5 X z)/ N) in case of individual series for direct method. in discrete series it is calculated as X Bar = E X / N.

Coefficient of standard deviation : this is a relative measure of the dispersion of series for examining the variation in different series. It is calculated as = o / X-Bar.

Coefficient of variation : It is the percentage expression of standard deviation and is used to compare the variability, homogeneity, stability and uniformity of two different statistical series. A higher value suggests greater degree of

.variability and lesser degree at stability. his calculated as : (o x XBar) x100 [1] --

Regression Analysis: In correlation analysis, the investigator is not concerned with gauging- the cause and.effect relationship even when it may exist between any two sets of a statistical series. This cause and effect relationship is studied through regression analysis. Regression Analysis describes the functional relationship which helps to make estimates' of one variable from another. It can also be said that it is measure of the average relationship between two or more variables in terms of the original units of the data.

Regression & Correlation

CORRELATION

Correlation is a statistical technique that shows the *degree and direction* of relationship between two or more variables. It is important because of the following:

- It measures extent of relationship between two or more variables which is important in statistics
- Predictions about expectations can be made. (say if there is proper rain, the food position is likely to be rood)
- Where value of one variable is known. the value of other variable can be worked out.

Types of correlation :

The important types of correlation may be positive (direct) and negative (indirect) OR linear and non-linear correlation. Other may be simple and multiple correlation OR partial and total correlation, OR logical and illogical Correlation.

Positive correlation : Where two variables move in the same direction i.e. if there is decline in one variable and 2nd variable also shows decline, the correlation- is direct or positive. For example at increasing price of a commodity, the supply of the commodity is likely to be increasing. Hence, between price and supply, the
correlation is positive.. -

Negative correlation : Where two variables move in the opposite direction i.e. if there is decline in one variable and 2" variable shows increase, the correlation is -indirect or negative. For example, at increasing price of a . commodity, the demand of the commodity is-likely to be decreasing.

Linear correlation : If change in one variable brings change in the other variable constantly at the same rate. over the entire range of values

Two variables are linearly related if there is a relation of the form Y = *a* + *b X,* between them.

Linear correlation is positive when the curve moves from *left to right upward* and negative when the curve moves from */ell to right downward.*

Non-Linear (or curvi-linear) correlation : If change in one variable brings change in the other variable constantly at the different rate, over the entire range of values
Two variables are non-linearly related if there is a 'elation of the form y = ax [2] *bx .-c = a.b'* between them.

Non-linear correlation may be positive when the curve moves from *left to right upward* and negative when the curve moves from *left to right downward.*

Degree and interpretation of correlation coefficient:

The coefficient of correlation lies between two limits i.e. + or— I. For perfect positive correlation, the value would be +1 and for perfect negative, the value would be -I . When value is 0, there is no relationship.

Methods for studying correlation:

There are broadly two methods i.e. *scattered diagram method and graphic method.*

Scattered diagram method: Under this method (which is also called dot diagram, datagram or scatter gram), the data is plotted in a graph in the form of dots. The term scatter means dispersion or spread of dots on the graph. Based on the spread of these dots, the correlation may be interpreted as under:

- Where the points are .close to each other, this shows high correlation but where these are not close, it means poor correlation.
- If the points show upward or downward trend, this means there is correlation. But if there is no trend,

it means variables not related or uncorrelated. Graphic method: Under this method (which is also called correlogram), the data is plotted in a graph paper on the basis of which two curves will be drawn. By observing the direction and closeness of these curves, it can be concluded whether the variables are related or unrelated. If they move in the same direction, it shows positive correlation. But if they move in opposite direction, there is negative correlation.

Algebraic or mathematical method : Under these methods the value of co-efficient of correlation remains between plus and minus I.

Under these methods there is Karl Pearson's Covariance method (or coefficient of correlation). This is based on arithmetic mean and standard deviation. The products of the corresponding values of two series i.e. co variance is divided by the product of standard deviations of the two series to determine the formula.

The calculation of covariance : It can be done both for individual data or grouped data by using direct method as well as short-cut method.

Direct method (when deviations are obtained from actual means) = r = Ely /N

where Yxy = Co-variance of x and y -

where x = (X —X Bar) means ..;,..riation in X series from its actual mean

where y= (Y — Y_eBar) means deviation in X series from its actual mean

where ox = Standard deviation of X series

where 6y= Standard deviation of Y series

Where N =No. of observations.

Measures to describe the degree of correlation

Coefficient of determination :

It the primary method through which the extent or strength of association is measured. It is calculated as: r^2 = I — (vi / v2)

It may be remembered that the coefficient of determination measures the strength of a linear relationship between two variable. If we have a lot of x, y points randomly scattered on the circumference of circle, there may clearly be relationship, but it is not linear: Hence, the coefficient of determination would be zero or close to zero.

Covariance : By computing the deviations of each point from the mean of x and y, we can obtain a measure of the direction and strength of the relationship. This can be done by multiplying these paired deviation together and then *add* the cross
products of the deviations over all the points.

Covariance = (X, Y) = I x'y' / n

Coefficient of correlation :A dimensionless value showing the extent and direction of relationship is coefficient of correlation.- It describes
how +Neil one variable is explained by the other. It can be calculated :

Coefficient of correlation = r {covariance (x, y) / o x o y}

REGRESSION ANALYSIS

The statistical technique .of estimating or predicting. Unknown value of a dependent Variable from the known Value of an independent variable, called regression :analysis If it is known that the two Variables say 'price (X) and demand (Y), are closely related, most probable value of Y can be found with given value of x. The regression analysis 'can be classified on the basis of: Change in proportion and Number of variables..

Regression on the basis of Change in proportion: On the basis 'of -change in proportion, regression can be Classified as *linear regression* and n*on-linear regression.*

Linear regression : When the dependent variable moves in a fixed proportion of the unit movement of the ... independent variable, it is called linear regression. When it is plotted on graph 'paper, it forms a straight line.. Mathematically it can be expressed as: - . .

yi.=.a.+bxi+ei (where *a* and *b* are known as regression parameters, *ei* denotes residual terms , xi presents value of independents variable and *yi is* the value of dependent variable say y when 'the: value of

independent' variable, that is x, is zero).

Again b denotes slope of regression line of y on x axis. *ei* denotes the combined effect of all other variable on Y axis.

Non-linear regression : In such regression the value of dependent variable say y does not change by a constant absolute amount for unit change in the value of the independent variable, say x. If the data is plotted on the graph, it would form a curve instead of a straight line. Hence it is called, curvi-linear regression.

Regression on the basis of no. of variables: Regression analysis can be simple, partial or multiple regression.

Simple regression : When only two variables are studied, it is knows as simple regression. One of these variables is independent and other the dependent. Functional relationship between price and demand of a product is an example of such regression.

Partial regression : When more than two variables are studied in a functional relationship but the relationship of only two variables is analysed at a time keeping the other constant it is partial regression.

Multiple regression : When more than 2 variables are studied and their functional relationship are simultaneously worked out, it is case of multiple regression. Study of growth in bank deposits in relation, to occupation and wealth of people, is an example of such regression.

Regression lines : It is a graphic technique to show the functional relationship between the two variables say X and Y i.e. dependent and independent. It is the line which shows average relationship between two variables X and Y.

Regression equation : These are algebraic expression of regression lines.

Properties of regression coefficient:

1 Both the regression coefficients bxy and byr cannot be greater than unit. In other words, the square root of the product of two regression coefficients must be less than or equal to +1 or -I.

2 Both the regression coefficients will have the same sign i.e. if bxy is positive, the byx will be positive.

3 If r is zero, then bxy and bp: shall be zero.

4 Regression coefficients are independent of change of origin, but not of scale.

Correlation and regression Relationship:

These are two important tools to study the functional relationship between variable. Coefficient of correlation is a measure of *degree of covariance* between x and y while the aim of regression analysis is to study the *nature of relationship* between the variable. This helps to knOw the value of one variable on

the basis of another,'

Correlation and regression: Difference

Correlation analysis tests the closeness of the variable while the regression analysis measures the extent of change.

- Con˙elation analysis studies the cause and effect relationship .between two variables but in regression analysis the causal relationship is studied.
- In correlation analysis there may be spurious correlation between variables but in regression, there is no such types of relation.
- Correlation analysis is a relative measure of linear relationship and the regression analysis is absolute measure.

Utility of regression analysis:

- It helps in predicting unknown value
- • It helps in establishing the nature of the relationship between two variables.
- It provides regression co-efficient which are generally used in calculation-of co-efficient of correlation.
- It is helpful in estimating the error involved in using regression line as the basis for estimation.

Limitation of regression analysis:

It is based on linear relationship, which on certain occasions may not be available.

- It is calculated on the basis of static condition of relationship.
- The relationship can be ascertained within limits only.

Standard error of estimates: It is the square root of the difference between the actual (observed) value and the estimated (computed) value of . independent variable. .

Time Series

Time Series : The statistical technique applied to measure the time based data over a period of time is known as time series analysis. It is a set of data and values depending on time. In other words Time Series is an arrangement of statistical data in accordance with its time occurrence. For example daily closing rate of stock market index, weekly position of the deposits and advances of a bank branch etc. Mathematically, a time series is expressed

Y *=f (i) where Y is the value of variable at time t.*

the values of a variable at time tl, t2, t3 ....tn are Y I, Y2, Y3 ....Yn respectively, the time series would be:

t =	t I	t2	t3 …….	tn
Y =	Y 1	Y2	Y3 …….	Yn

Time series has two variables one of which shall be time, the independent variable and other; a dependent variable Y, at different points of time. The value oft may be hourly, daily, weekly, monthly, quarterly, half-yearly or yearly. The time series are generally studied with the help of diagram, where time is shown on X-axis and the quantity variable on Y-axis.

Objectives : Time series helps in review of current achievements, study the past behaviour, facilitate comparison, predict future behaviour, forecast the trade cycle etc.

Components of time series : Value of time series shows various types of fluctuations (also called variations er the movements). A time series has components such as secular trend or long term variation, seasonal variations, cyclical variations, irregular variations or random variations

Secular trend : It refers to general tendency of the time series data to increase,¯decrease or remain constant during a long time period. Hence a general rise in time series is a secular trend. The trend can be upwards or downwards. It can be linear (when rate of change remains constant) or non-linear (where rate is not constant).

Seasonal variations: Seasonal variation in a time series will be there if the data are recorded quarterly, monthly, weekly, daily etc. In a time series data, where only annual figures are given, there are seasonal variations. Consumption, production of commodities, interest rates, hank clearing etc. are marked by seasonal variations.

Cyclical variations: In some time series, there may be periodic up and down movements in-economic data which are called cyclical variations. These cycles are repeated at time intervals ranging from about 3 to 10 years. Cyclical variations help in formation of a business policy, estimate of future behaviour, ideal of irregular fluctuations etc.

Analysis of time series:

As per classical time series analysis, multiplicative relationship between four components of time series (i.e. trend, seasonal components, cyclical components, irregular components) is assumed. Accordingly:

O = T x S x C x I (where O stands for original data, T for trend, S for Seasonal component, C for cyclical component and 1 for irregular component.,

Example : If T = 800, S=1.4, C=I .5 and 1=2.6; then O= 800x I .4x1.5x2.6 = 4368

In another approach, each observation' of time series is the *sum ofthese four components:*

O = T +S+C+I

Example : If T.= 800, S=50, C=30 and 1= -40, then O = 840

Measurement of trend:

There are various methods for measurement of trend component in a time series that include graphic, semi averages & moving averages and least squares or curve fitting by principle of least squares.

Graphic or free hand curve fitting method:

It is the simplest method and consists of following steps:

- Obtain a histogram' by plotting time series value on a graph paper
- Draw a free hand smooth curve through the points and then a straight line on the basis of judgement.
- It would show the long term tendency of the data.

Semi averages method:

Secular trend can be obtained by semi-averages by dividing the original data into two equal parts. The value of each part is summed up and then averaged. The average• of each part is centred in the period of time of the part from which it has been calculated and then plotted on the graph. A line is drawn to pass through the plotted points.

Moving averages method: It includes averaging of seasonal and other short term variations from the series so that only trend is left in the series. The nn. of items taken for averaging will be the no. required to cover the period over which the fluctuations occur. This average is taken as the normal or trend value for the unit of time falling at the middle of the period covered in the calculation of the average. The averaging gives a smoother curve, reducing the influence of the variations that pull the annual figures away from the general trend.

Least Square method:

This mathematical method is widely used with the help of which a trend line is fitted to the data in such a way that the two conditions are satisfied i.e.

1. E (Y-Yc) = 0 (i.e. the sum of deviations of the actual values of Y and computed values of Y is Zero)
2. E $(Y-Yc)^2$ is minimum. (i.e. the sum of squares of deviations of the actual and computed values is minimum from this line. It is for this reason that the method is known as least squares method.

This line which we get by this method is Called. Line of BeSt Fit. The straight line trend is shown by the equation: .

YC = a + bX. (Yc is the trend value to distinguish from the actual Y values, *a* is the intercept of the values of the Y variables when X = 0, *b* is the slope of the line, X refers to time.

PROBABILITY DISTRIBUTION

Probability implies likelihood. It is related to making estimates. When the happening of an event is certain, the probability — l and when the happening is impossible, the probability = 0. In the first case P=1 and in the 2nd case P = 0. For example, if a coin is *tossed,* the pv babability of head or tail is V2 but actually for a 10 times tossing, the actual no. of heads or tails may be different.

The theory of probability is widely used in the filed of statistics, economics, commerce etc. that involves making predictions in the face of uncertainty. Probability is expressed in the form of fraction, a percentage or a decimal.

Probability distribution : It stands for listing of probabilities for every possible value of a random variable. The concept is similar to actually observed frequency distribution. Probability distribution tells as to how the total probability of 1 is distributed among the different values which the random variable can take.

Estimates : Two types of estimates can be made about the population (the field about which estimates are to be made), a:point estimate and interval estimate.

A point estimate is a single number that is used to estimate an unknown population parameter: A bank branch manager estimates that as on Mar 31, the deposit of his branch will reach a level of R.S.15 crore. A point estimate is not sufficient as the outcome may be right or wrong. The outcome may be 95%© or

may be 75% of-the estimate. In other words the error is 5% and 25% in this case. A point .estimate -can be useful, if it is accompanied by an *estimate of error.*

An interval estimate is a range of values that is used to estimate a population parameter It indicates the error by the .extent of its range and by the-probability of the true population parameter. In the above example, 'the branch manager may estimated the deposits between a range of Rs.14cr to Rs.16 cr.

Estimator: A sample statistics used to estimate a population parameter is called estimator. The sample mean x can be an estimator of the population mean *i.* Sample proportion can be used as an estimator of the

population proportion. An estimator should be unbiased, efficient, consistent and sufficient.

Estimate: It is a specific value of a statistic. For example if vehicles department of a bank observes mean mileage of 1.50 lac km of its cars of a particular make, the department can use this, for the whore fleet of cars of that make, which becomes an estimate.

Linear Programming & Simulation

Linear programming is a mathematical technique for allocating scarce resources in an optimum manner. The word linear means that the relationships are represented by straight lines and the word programming means a procedure that is used to get the best solution to a problem that involves limited resources. There are certain important aspects concerning linear programming such as:

Decision variables like products, services etc. compete with eachfor scarce resources. These variables should not have negative values. If a bank provides three services, the non-negativity condition would be RA > C, RB.> 0 , RC> 0. This means that these products are being rendered or not rendered. But it cannot be negative. There must be proportional relationship between the variable to give the linearity. The no. of activities should also be finite.

Basic variable: The non-zero variables in a basic feasible solution are called, basic variable.

Slack variables: If a constraint has a sign <, something positive has to be added to the left side to make it, equal. The positive variable, that is added is, called slack variable.

Surplus variable: If a constraint has a sign >, something positive has to be subtracted from the left side to make it equal. The positive variable, that is added, is called surplus variable.

Steps : Formulation of Linear Programming problem, involves the following steps:

1. Identify the unknown variables to be determined and assign symbols to them.

2. Identify all the restrictions or constraints in the problem and express them as linear equation or inequalities of decision variable.

3. Identify the objective or aim and represent it also as a linear function of decision variables.

Problem *: A firm manufactures two types of cables i.e. general use cables and special use cables. The general use cable takes one man hour per meter and the special use cable takes double time than the general use cable. The firm has available 3000 man hours per day. Raw material is adequate to manufacture only 2500 metres of cable per day. The special use cable also requires special enameling for which the facility is available for 800 metres per day.*

Make out a linear programming problem (LPP), to maximize the profits, if the profit from general use cable is Rs.4 and from special use cable, it is Rs.6 per metre.

Solution:

Let us assume the production of general use and special use cable is xi units and x2 units respectively.

Hence, Profit function Z= 4xi and 6x2_

The maximum man hours per day are 3000 and *man* days per day requirement is xi + 2x2. Hence. x I + 2x2 < 3000.

Raw material is available for producing 2500 metres xi + x_2 < 2500

Enameling facility is available for 800 metres per day for special purpose cable: x2 S 800

.

Hence,. **the LPP** would be 4xi and 6x2_

Subject to: x I 2x2 < 3000, xl ± x2 < 2500, x2. < 800 and xi + x2 > 0 (non-negativity constraints).

Solution of linear programming problems:

Two methods are generally used for.the solution i.e. Geometrical (or graphical) method and Simplex method.

Geometrical (or graphical) method : This method can be used where Z is function of 2 variables only as with increase *in* variables, the calculations become complicated.

The following steps are involved:

Step-1: formulate linear programming problem by restating the given information in mathematical form i.e. an equation for the objective function.

Step-2: plot the constraints on the graph.

Step-3: identify feasibility region and ascertain coordinates for its corner points.

Step-4: test which corner point is most suitable. Find a point in the permissible region as obtained in Step-3,that gives the optimum value of Z

Simplex method: This technique also known as Simplex Algorithm is an iterative procedure (i.e. doing repetitively) for solving a linear programming problem in finite number of steps. The method is an algebraic procedure that progressively approaches the optimal solution. The method assumes that the variables are **non-negative**. The value of the objective function is increased at each step of iteration till further improvement is not possible. The method begins at the point of no production or zero solution. It involves the following steps:

Step-1: Write the program relating to the given. problem.

Step-2: To eliminate the inequalities add *slack or surplus* variable and rewrite the program.

Step-3: Determine the first basic feasible solution by starting at the origin (i.e. starting with zero solution)

Step-4: Write the initial simplex Tableau 1

Step-5: Calculate Z j (which is inner product of cj and xi)

Step-6: Calculate Zj Cj and select the greatest absolute value with negative sign in index row

Step-7: Highest number with negative sign determines the key column and also determines the Entering variables.

Step-8: Develop ratio column where R = bi / ai.) for the column of entering variables.

Step-9: Select the least, positive ratio (or value of R) and determine **the exiting** variables. The row containing the least positive ratio is the key row and variable corresponding to it is the exiting variable.

Step-10: Determine the key figure which is the number at the intersection of the key column and key row.

Step-11: Obtain new tableaus for entering variable, divide the figures in the row of leaving variable by key figure.

Step-12 Repeat the step 5 to 11, till no negative numbers exist in the index row.

Maximisation problems : Simplex method is suitable for the solution of maximisation problems such as profit maximization or product maximization. The iteration process given above gives the requirement of maximization problem. Constraints here are of type S.

Minimisation problems: Where the constraints are of the type = or > signs and the objective function may be of minimization (say cost reduction, time reduction), the above method is used with certain modifications.

Primal problem : It is the original problem in the linear programming problem.

Dual problem : it is the other linear programming problem intimately related to the original problem.

Either of these problems can be primary problem, where the other will become dual problem.

Importance of linear programming :

I It can provide insight into problem situations.

2 It leads to optimum utilization of productive factors by providing information base_

- 3 Different solutions are generated and best could be adopted by the management.

4 Bottlenecks in the production process can be identified for removal.

5 It introduces- an element of flexibility in analysis of variety of multi-dimensional

Limitations of linear programming

1. It assumes linear .relationship between variables, but in real business situations, the Constraints may not be expressed linearly.

2 LP does not take into account the effect of time and uncertainty.

3 Parameters in LP are taken as constants but in real situation, that is not, the case.

4 Solutions provided by **LP** are good in static conditions and not 'in dynamic situation because the effect of Time is not taken..

Application of linear programming:

It can **be** used in various applications such as;

1 Management applications -: Portfolio selection, staffing problem, -profit planning, equitable salaries, traveling sales Man problems, finance mix strategy, media selection etc.

2. Administrative applications**:** Optimal .use of resources, work allocation for optimal efficiency, evaluation of various schemes.

3 Industrial applications : Product mix, blending mix, production scheduling, trim loss, transportation problems.

4 Non-industrial applications : Agriculture, contract awarding, environmental protection.

Simulation

Simulation : Simulation is the method of studying the effects of changes in the real system through models. A model is manipulated to know the end result. The method is more appropriate to situations where the size and/or complexity of the problem makes the use of other techniques difficult or impossible.

Use of simulation : The simulation can be used in Air traffic control queuing, air craft maintenance, assembly line scheduling, inventory order designing, rail freight carriers, facility layout etc.

In a simulation model, the system's elements are represented by arithmetic, analog or logical processes that can be executed, to predict the dynamic properties of the real system. In this model, the time can be increased by fixed time increments (say on hourly, daily, weekly basis) or variable time increments. At each point of time, the system is scanned to determine if any event has happened. Then the events are simulated and time is advanced. Time is advanced by one unit, even when the events do not occur.

Why use simulation? : Some situations do not lend themselves to precise mathematical treatment. Others may be difficult, time-consuming, or expensive to analyze. In these situations, simulation may approximate real-world results; yet, require less time, effort, and/or money than other approaches.

How to Conduct a Simulation

The steps required to produce a useful simulation are presented below.

1 Defining the problem (i.e. define objectives and variables)

2 Construct the simulation model (specify the variables, parameters, decision rule)

3 Specify the values of parameters and variables.

4 Run the simulation (determine the starting conditions and run length)

5 Evaluate the result and propose new experiment. (determine statistical tests and compare with other information).

Advantages:

Simulation is useful where the experiments on real system (a) would disrupt ongoing activities (b) would be too costly to undertake (c) require many observations over an extended period of time (d) do not permit exact replication of events and (e) do not permit control over key variables.

It is preferable when a mathematical model (a) is not available to handle the problem (b) is too complex (c) is beyond the capability of available personnel (d) is not robust enough to provide information on all factors.

Disadvantages :

I. It is time consuming

2. It requires computer experience and expertise on the part of the user

3. There are very few principles to guide the user in making decisions on what to include in the model and the length and no. of simulation runs. The user has to use his intuitive judgment.

Module: C

HRM in banks

SYLLABUS

Fundamentals of HRM, development of HRM in India, Relationship between HRM and HRD, Structure and functions of HRD, Role of HR professional, Human implications of organizations; training and development, attitude and soft skills development, role and impact of training, career path planning and counseling, employee behaviour, theories of motivation and their practical implications, role concepts and analysis, self development., Performance Management and appraisal systems; Reward / punishment and compensation systems., HRM and Information Technology, information and data management, knowledge management.

FUNDAMENTALS OF HUMAN RESOURCES MANAGEMENT

Human resources management has been one of the most important task of any organization that has bearing on its performance.

People management is dynamic and always remains a 'live' issue. On the other gand, the technology get stabilised at least for certain period in its evolution process, due to which it is passive. Human affairs in any organisation are influenced by a wide variety of emotions like love, hate, needs, expectations, values, beliefs, traditions and changes in social, political and economic field.

Organisation — Organisation is the rational coordination of the activities of a no. of people for the achievement of some common explicit purpose or goal through division of labour and through a hierarchy of authority and responsibility (Schein, 1979).

From labour management to Human Resources management: Different phases : With the Industrial Revolution, there was a need for separate departments like finance, accounting, production etc. But the process of HRM saw three distinct phases.

Phase-1: Conventionally the HRM received little exclusive attention of HR was deemed to be acquired and managed easily. In this phase, the HR function revolved round the functions such as time keeping, wage administration etc. A new dimension of bargaining between the Unions and the management during the Industrial Revolution gave rise to creation of departments like Labour Deptt. In 1902, the National Cash Register Company established labour deptt. In this phase, the organizational maintenance goal, as such, was not widely recognized or accepted, except among a limited group of individuals.

Phase-2: Personnel Deptt. in this phase looked like the one in 7os. The major area continued to be selection, training, methods, improvement and employees welfare. In this phase, the focus went beyond the '9 to 5' concept of work and included long term issues. The outlook also changed from mere 'labour' to 'person'. In this phase proper attention was given to development and administration of systems for:

1. Acquisition (i.e. recruitment and selection)
2. Integration (i.e. induction training)
3. Training and placement (formal or on the job training)
4. Compensation (incentives, welfare schemes, medical benefits, long term benefits)
5. Promotion (reward for good performance)
6. Evaluation (performance record).

Phase-3: In this phase, a new thinking on motivation was getting consolidating based on McGregor's Theory X and Y (explanation of organizations), McClelland's work on Achievement motivation, Herzberg's Motivation- Hygenic theory and Argyris work on job contents. Hence the 7os and 8os witnessed the emergence of this phase with emphasis on people management. The organizations adopted the developmental approach characterized by humanistic-participative value. Career planning and succession planning have evolved as mechanisms of growth for the individuals and the organizations.

Authors and their work related to HRM :

1. Peter Drucker (in the book Land Marks of Tomorrow) - no matter how much we can quantify, the basic phenomenon are qualitative ones such as change, innovation, risk, judgement, dedication, vision, reward and motivation.

2. Robert Owen (1771-1858) — Best investment of organisation is in worker (he called vital machines)

3. Charles Babbage **(1792-1871) — A** professor of mathematics an advocate of division of labour. He believed in applying scientific principles to work processes for increasing productivity and reducing expenses.

4. Frederick Taylor (1856-1915) — He is famous for his concept of Division of Labour **and** Time & Mother studies.

5. *Grant and Gilberths* — **They substantiated Frederick Talylor's concepts.** Major assumptions of approach of Frederick **Talylor are:**

Task can be broken down to simple units for people to understand and perform

People do a given activity in return for money.People will have to do what is defined by organisation and in turn by technology.

This approach ignored vital aspects of human behaviour (1) it concentrated on activities related to work only

and bahaviour aspect not taken into account.

6. Elton Mayo and others at Western Electric Company (1924-33) — Impact of Human Studies is landmark in evolution of management thought and human approach in management.

7. Researchers like Chris Argyris, A. Maslow, Douglas McGregor and Fredrick Herzberg — Highlighted dimensions of motivation. **Development of people management function :** The history of management of

people as a distinct managerial function goes back to end of 19th century and beginning of loth century when there was significant increase in no. and size of organisational units. In India, the experiment of group behaviour in Ahmedabad Mills by Prof. AK Rice (1952) is a significant contribution.

HRM & HRD - STRUCTURE AND FUNCTIONS

Human resources management of an organisation is often an independent department composed of various sections including recruitment and retention, performance and appraisal management, HRD *and* compensation sections. HRM refers to the art of managing *all aspects* of the human workforce in an organization. It aims at providing an optimal working environment for employees to fully and freely utilize their skills to their best to achieve the organisational goals. HRD is sub category of **HRM** which focuses on 'nurturing' employee's skills. **HRD** aims at developing a superior workforce so that the company and individual employees may achieve their work goals in the customers' service. There is no conflict between the structure and functions of **HRM** and **HRD.** The routine functions are part of HRM and HRD function emphasizes on organisational interventions for climate development, employee development & organisational development, linked with organisational goals. *Change of nomenclature of department relating to human resources management:*

1st stage - Labour and welfare department, 2nd Personnel department & 3rd HRM department

Components:

The conventional components of people management are categorized under Personnel Administration.

The system related to acquisition, promotion, administration, salary and long term benefits are covered under administration.

The traditional labour management, grievance and discipline management activities are covered under maintenance systems.

The development systems such as induction, development and growth, performance appraisal and counselling, career planning are covered under HRD.

There is no conflict between the structure and functions of HRM and HRD. The difference is only in the approach and emphasis. HRM assumes that the management of people is an integral part of the resources management task within organization for achievement of organizational goals. HRM focuses on developing people related system. Hence routine functions become part of HRM.

On the other hand, the HRD functions emphasize on climate development and change management process. The focus of HRD is on overall organizational development process which also include development of people.

ROLE OF HR PROFESSIONALS

With the passage of time, the role of HR professional came to be known as a specialized job — a staff function. Individuals having special qualifications and skills joined the organizations as specialist professionals. Shaphard (1977) summarized the role and qualification of HRP in different phases:

1945-65 : About so year old., ex-army or civil service background, meticulous and systematic but not innovative.

1966-75 : About 40 year old, ex-teacher having some training background, having no experience in production or such organizational functions. He does not have influence or credibility with top or line management.

1975-85 : About 3o year old, reporting directly to CEO, widely read, innovative and receptive to change. He may be member on the Board. Acts as facilitator.

Personnel Functions and responsibilities of line and personnel managers

Function	Line management responsibility	Personal Deptt. responsibility
		Role analysis, administering

Recruitment and selection	Provide data for job analysis and specify desired skills	recruitment and selection, complying with legal and organizational rules.
Retention	Interview candidates and decide	Fair and consistent policies and practices
Training & development	On-the-job training, coaching etc.	Career planning and organizational
Performance appraisal	Performance and potential appraisal, counseling	Development of performance appraisal system, maintenance of personal records and
Grievances	Handling grievances	Setting up grievance procedures, monitoring and recommending_policy
Discipline	Responsibility to manage discipline_	Advice on disciplinary rules.

ATTRIBUTES OF HR PROFESSIONALS

Technical attributes:

1. knowledge of performance appraisal system and their functioning
2. knowledge of potential appraisal and mechanism of developing a system.
3. Knowledge of various tests and measurement of behaviour
4. ability to design and coordinate training program at worker and supervisory level
5. Professional knowledge of personnel and management
6. Knowledge of behavioural sciences
7. Understanding of overall organizational culture.
8. Knowledge of career planning, processes and practices
9. Knowledge and skills in counseling

Managerial attributes

10. Organising ability
11. Systems development skills

Personality

12. Initiative, imagination and creativity
13. Positive attitude towards others
14. Concern for excellence
15. Ability to work as a team member.

HR function in Banks: It is not generally performed professionally. HRD is considered a generalist discipline. CII developed an HR Competency Model in 2004 that listed 19 inter-linked competencies for **HR** heads. These includes behaviourial competencies (such as communication, initiative, drive, creativity, self confidence, teamwork, influence, problem **solving** and inter-personal skills), which have been embedded in io functional competencies (such as business knowledge, change management, diversity management, service orientation, execution excellence, financial perspective, building expertise, personal credibility, relationship management and strategic thinking and alignment).

Role of HR professional in future (as per Ulrich): a partner with senior **and** line managers in strategy execution, helping to move planning from board room to market place an expert in the way work is organised and executed.A champion for employees representing their concerns to senior management and working to increase employee contribution.An agent of continuous transformation, shaping processes and a culture that improve an organization's capacity for change.

What should the HR professional do ? acquire additional professional qualifications relevant to their role.Holding regular meetings of study circle. Exchange ideas with personnel fraternity from different organisations. Association with and participation in activities organised by other professional bodies. Interaction between **HR and** technology experts & Undertake problem based project studies.

Things to remember: 1. The role of HR functionaries has undergone qualitative change HR functionaries have total responsibilities about the management of human resource in the organization. 2.HR functionaries are responsible for development of HR related systems.HR professionals must have

qualification in HRM. Line managers should not meddle with the management of HR.

DEVELOPMENT OF HR FUNCTIONS IN INDIA

In India, by the 6os, the demand for personnel professionals start emerging. Around that time, institutions like Indian Institute of Personnel Management (IIPM) and National Institute of Labour Management (NILM) were established.

The objective of establishing IIPM was to develop and spread the ideas concerning the human values and serve as a forum for exchange of ideas and experiences and collection and dissemination of the principles, practices, techniques and methods regarding Personnel Management.

The objective of establishment of NILM was to encourage and promote the development of cordial relations between the employers and employees, conduct investigations in to different labour problems, undertake study of existing labour legislation for improvement, organize training and instruction in personnel management.

Later on these two bodies were merged as National Institute of Personnel-Management during 1982.

In the earlier phases, India had visionaries like JN Tata who established TISCO at Jamshedpur. This organization took a no. of steps in the area of HRM based on which, some of important legislations were later on passed in India. These initiatives of TISCO and following legislations are as under:

Aspect / Area	By TISCO	Enforced by	Name of the Act
8-hour working day	1912	1948	Factories Act
Free medical aid	1915.	1948	ESI Act
Establishment of Welfare Deptt	1917	1948	Factories Act
School facilities for children	1917		
Formation of committees for handing complaints concerning service	1919	1947	Indl. Disputes Act
Leave with pay	1920	1948	Factories Act
EPF Scheme	1920	1952	EPF Act
Workmen's Accident compensation	1920	1923	Workmen's Compensation Act
Tech. Institute of apprentices, craftsmen and engg. Graduates	1921	1961	Apprentices Act
Maternity benefits	1928	1946	Bihar Maternity Benefits Act
Profit sharing Bonus	1934	1965	Payment of Bonus Act
Retiring gratuity	1937	1972	Payment of Gratuity Act

In addition to the above, the other provisions of law include:

1. Article 16(1) of Indian constitution — provision for equal opportunity for employment.
2. Employment Exchanges (compulsory Notification of Vacancies) Act 1959 — required the employers to notify the vacancies
3. Apprentice Act 1961 — provision for training linked to employment
4. Child Labour Act 1986, Bonded Labour System Act 1976, Inter-state Migrant Workmen Act 1979 — for safeguarding the interest of specific groups.

In 1980s, the Govt. started introducing employee participation and allocating shareholding to workers. HRD as a sub-system of HRM emerged as a feature.

Qualitative difference between Personal Function and HR System (as per Pareek & Rao)

Personnel Function	Human Resources System
An independent function	A sub-system of a larger system i.e. organization
Main task to respond effectively to the demands	Main task is to develop enabling capabilities (pro-
Main responsibility for personnel matters	All managers share the responsibility of HRM
Main emphasis on personnel admn. or	Main emphasis on developing people and their
People are motivated by salary and reward	**Peo**ple are motivated by challenges **and opportunities for development and**

In the gos few organizations such as Larsen & Toubro, BHEL, MARUTI, HDFC etc. started using innovative

practices. Among Indian banks, SBI, BoB, Canara Bank also took initiatives in HRM.

Other developments in India:

- Establishment of National **HRD** Network during 1985
- Establishment of Indian Society for Traing & Development in 1970
- 5th 5 Pay Commission that made recommendations for making performance appraisal open, improvement in motivational skills etc

HRM & INFORMATION TECHNOLOGY

Globalisation has removed all the physical and national boundaries by linking organizations from all parts of the world, by use of IT. FIRM as a function has dual responsibility to respond to the developments having taken place in the area of information technology (IT), for transformation of the mind set of all individuals across the organization and also use of IT in day to day decision process. The banking sector has absorbed maximum technology for their operations. IT has offered a variety of delivery channels to support customers' needs in an efficient and effective manner.

Role of IT in HRM

There is lot of scope for use of IT in whole range of FIRM functions i.e. recruitment, training, placement, appraisal and reward system, organizational development initiatives etc.

The need for use of IT can be seen through the following:

1. Basic information about employee used within the organization.
2. New dimensions have been added to employee data such as training, competencies, skills, expectations etc.
3. Up-dation of employees data
4. HRD decisions are data-based now and IT provides that data.
5. Adherence to statutory requirements.

As per Nadler:

1. Massive influx of technology into workplace presents great challenge in keeping the workforce's work and knowledge base current and avoid workforce obsolescence
2. New tools disrupt traditional work patterns and can have demoralizing effect. HRD effort must align to the corporate planning.
3. HRD efforts would be examined in terms of contributing to high performance work unit and demonstrating results.
4. Massive influx of technology into workplace presents great challenge in keeping the workforce's work and knowledge base current and avoid workforce obsolescence
5. New tools disrupt traditional work patterns and can have demoralizing effect. HRD effort must align to the corporate planning.

6 . HRD efforts would be examined in terms of contributing to high performance work unit and demonstrating results.

HR Information and Database Management

A computer based data can enhance the quality of decision making. A typical HR information system includes the following types of data: The need for use of IT can be seen through the following:

1. Bio-data
2. Educational qualification
3. Professional qualification
4. Organisational history (entry level, promotion, placements, training, performance appraisal, competencies).
5. Salary & allowances.

The above type of data, requires few changes over a time period. But the data base provides lot of information as input for decision making.

HR Research

Research in FIRM can be undertaken to understand:

1. trends of existing systems like recruitment, promotion, training, appraisal system etc.

2. to understand the workforce in terms of motivation, commitment, expectation, frustration etc.
3. to remain sensitive to internal environment, regular opinion surveys, benchmarking, climate studies etc. can be conducted.

Knowledge Management (KM)

KM refers to process of (a) creating, (b) storing (c) distributing and (d) pooling the knowledge (as per Wilcox-[1]997)-

The people in a system are the sources of creating knowledge while storing and distributing the information is the responsibility of the information technology machinery of the organization.

Hence management of 'knowledge worker' is very critical issue and cannot be done by traditional, bureaucratic process.

Knowledge management has gained prominence in the light of the uncertainty that the employee who has created the knowledge, will continue with the organization or not, particularly where the attritions levels are higher.

DEVELOPMENT OF HUMAN RESOURCES

People in an organization cannot be treated like other factors of production. Hence, after originating as a set of activities, HRM has over the years, acquired a status of a crucial function of the organization. It has been recognized that there is linkage between the individual's satisfaction and organisation's growth.

HRD & its sub-systems

HRD means organized learning experience in a definite time period to increase the possibility of improving job performance growth (Nedlar-1984).

Organisations set goals and direct their efforts to achieve these goals. These goals may be in terms of production, finance, sale, control or monitoring of people. The organizations have structure to manage the entire process. This structure is the edifice around which the processes are built. Each unit of this sub-system requires certain knowledge, skills and attitude in an individual.

Hence for ensuring performance of the individuals it is essential that:

1. Individuals has the knowledge as to what is expected of each unit / level.
2. Individuals have the required capabilities to do what is expected
3. Mechanisms are available to measure what is expected.

According to Nadler, HRD is a process, by which the employees are helped in a continuous and planned way to:

1. Acquire or sharpen capabilities required to perform various functions associated with their present or expected future jobs.
2. Develop their general capabilities as individuals and discover and exploit their own inner potentials for their own and or organizational development purposes.
3. Develop an organizational culture in which supervisor-subordinate relationships, teamwork and collaboration among sub-units are strong and contribute to professional wellbeing.

Sub-systems: The sub-systems that can be developed include:

1. Training and development
2. Performance appraisal, feedback and counseling
3. Potential appraisal, career planning
4. Organizational development
5. HR information system

HRM has three sub-systems viz. administrative, developmental and maintenance.

Job analysis : It is a technique that facilitates the listing of what is required to perform a task. It comprises of job description, job specification and ob evaluation.

Job description	To record each and every activity an individual is to perform in a given set-up
Job specification	A list of requirements in terms of educational qualification, age, work experience, specific knowledge, skills, expertise, temperament etc.
Job evaluation	Used to compare similarity between jobs within an organization or between organizations or even in an industry.
Task	A basic element of a job and requires a person to achieve a specific product.

Job	A complex system of task requiring an individual to achieve an overall product and still making the relationship relevant.
Position	It puts an individual in hierarchical pattern expecting those below to report or surrender to higher positions and conform to their expectations while those higher up, may be led to exploit the relationship and demand conformity.
Role	It emphasizes the pattern of mutual expectation
Work	It involves still complex pattern as it goes beyond to encompass sotto-psychological relationship.

Training & Development - Role & Impact of Training

The objective of training and development is to comprehend how this concept of learning could be applied to the organizational context. Establishment of training and development system as part of the HRD effort involves (a) identification of training needs (b) conducting of the training (c) evaluation of training and (d) selection and development of trainers.

Objective of Training and Development:

Employees should be provided with learning opportunities to enable the organizations and individuals to achieve their goals. The organizations have to analyse their requirement. The need of the organization can be linked to the career progress of the individuals that could lead to:

1. Improved performance of the individual on his present job.
2. His preparation for an identified job in a not-too distant future.
3. His general growth not related to any specific job.

Training : It is the learning related to the present job. When goal is to improve performance, it should be conducted and evaluated to check the improvement.

Education: It is the learning to prepare the individual for a different but identified job. If the goal is futuristic, it would be required to be provided.

Development : It is the learning for growth of the individual not related to a specific present or future job. No direct impact may be seen on the performance.

Theories of adult learning:

Lindeman's work was the first instance of defining the perspective of adult learning. It is defined as a cooperative venture in non-authoritarian & informal learning, the chief purpose of which is to discover the meaning of experience, a quest of mind which digs down to the roots of the pre-conceptions which formulate our conduct.

There are a no. of theories to explain as to how we learn. Nadler categorizes them in three sets:

Mechanistic (or behaviouristic) theories *:* learner is passive in the process of learning. Learning occurs only when a learner is conditioned to give the right response.

Cognitive theories : The purpose of learning is to teach the brain to engage in such critical thinking and problem solving.

Organismic (or Humanistic) theories — Learning occurs when learners have the freedom to learn what is particularly relevant to their personal life situation.

As per Decenzo and Robbins:

1. Learning is enhanced when the learner is motivated.
2. Learning requires feedback.
3. Reinforcement increase the likelihood that a learned behavior will be repeated.
4. Practices increase a learner's performance.
5. Learning must be transferable to the job.

APPROACH TO TRAINING

For proper training, a systematic approach has to follow certain logical processes for enhancing knowledge, skills and attitudes of their personnel, which include:

Step 1 — Analysis and identification of training needs.

Step 2 - Preparation of a training plan

Step 3 — Conduct of the training program which includes designing the program in interms of the time, duration, target group, sequence of inputs and methodology. The teaching methodology include readings, lectures, experimental lectures, discussion, participation training, case studies, role plays.

Step 4 — Evaluation of the training program and the plan (there are various levels for evaluation i.e. reaction level, learning level, the behavior level, functioning level).
Step 5 — Selection and development-of trainers.

ATTITUDE DEVELOPMENT

Attitude can be defined as a persistent tendency to feel and behave in a particular manner towards different situations.

Components: Attitude has three basic components i.e. emotional, informational & behavioural.

Emotional component : This involves person's feeling that may be positive or negative.

Information component : A belief may be founded on insufficient observation or information or opinion. A branch manager is of the opinion that a 2 weeks' training may be adequate for a person to work effectively as a System Administrator, which actually may be 4 weeks. The belief of the manager represents his attitude toward training.

Behavioural component: It consists of person's tendency to behave in a particular way towards the object. The behaviour of the manager in the above situation has impact on the workplace.

Significance of attitude at workplace

Attitudes help predict work behaviour. It also helps people adapt to their work environment. Attitude serve 4 important functions:

1. The adjustment function — which helps a person to adjust to his work environment.
2. The ego-defensive function — which helps a person to defend his self-image.
3. The value-expression function — which helps a person with a basis for expressing their value.
4. The knowledge function — which helps a person to organize and explain the world around.

Changing attitude:

Though it is difficult but it is not impossible to change the attitude of the people. The major barrier against such change are prior commitments and lack of information. These barriers can be come over by providing new information, by resolving the discrepancies between attitude and behaviour. To an extent, the change is possible by co-opting i.e. getting people involved in improving the things.

CAREER PATH PLANNING

Individuals expect certain changes or advancements to take place in a time bound period and when such changes do not occur, they get frustrated or aliened.

Erik Erikson has divided life into 8 stages (4 in childhood and 4 in adulthood). The adulthood stages are relevant in understanding, as to what the individuals expect in the organizational careers. These stages are:

Adolescence — where individual's development is to achieve an ego identity.

Young adulthood — where the individual starts developing relationship with individuals, groups or occupation.

Adulthood — where the individuals starts guiding the next generation and passes on values and knowledge to others.

Maturity — where the individual attempts to achieve ego integrity.

Levinson's age-specific transitions correspond to Erikson's 4 adult stages.

Dalton, Thompson and Price have emphasized roles and-relationship, an individual may experience in the 4 career roles such as :

(a) apprentice — this is beginning of the career. Individual is doing routine work at this stage.
(b) colleague — beginning of making an independent contribution.
(c) Mentor — where individual develops ideas, manages others and
(d) Sponsor — individual broaden his perspective and think long term as he is now a part of the top management.

Career pattern

Driver (1985) has listed these patterns as CAREER CONCEPTS. These include:

(a) Linear career — where the individual enter into an occupation and plans for upward movement using the organizational hierarchy.

(b) **Steady state career — where the individual enters into an occupation, acquires skills but decides not to move upward.**

(c) Transitory career — where individuals shift to new jobs.
(d) Spiral career — where individuals shift to new jobs, move up in status and rank.
Schein has given another framework of 3 dimensional movement i.e.
(a) vertical i.e. along with the hierarchy
(b) circumferential — along with the different divisions and functions
(c) radial towards the centre of the organization.
In a bank situation, three types of movements may be as under:

Vertical Movement

Scale	Management level	Minimum years of experience before promotion to next grade
I	Junior Management	7 years **Now Changed to 3-4 years in all**
II	Middle Management	5 years Top Top
III	Middle Management	5 years
IV	Senior Management	3years
V	Senior Management	2 years
VI	Top Management	2 years
VII	Top Management	2 year

Horizontal movement

Branch size	Branch Manager	Major business dimensions
Small	Scale 19MG)	Personal Banking, agriculture, priority sector
Medium	Scale II (MMG)	Personal Banking, agriculture, priority sector, commercial credit
Large	Scale IIISMMG)	SSI, Industrial and institutional credit
Very Large	Scale IV-V (SMG)	SSI Industrial institutional credit and forei n

Inclusion movement

Office	Management level	Responsibilities
Regional office	Scale III	Incharge of Functon like credit, staff, development & inspection
Regional office	Scale IV (Regional Manager)	Coordination, control and development of the region
Zonal Office	Scale IV (Chief)	Incharge of functions like credit, staff,development, inspection
Zonal Office	Scale V Scale VI (Zonal Manager)	Coordination, control and development of the zone
Central Office	Scale IV — Chief Manager	Head of functions like credit, staff, development,
Central Office	Scale V — AGM	Overall supervision and policy review function
Central Office	Scale VI — DGM	Overall control and policy review for modifications
Central Office	Scale VII — General Manager	**Strategic management for a function :review,change**

Career Anchors:
This concepts refers to a personal sense of type of work individual wants to pursue and what that work implies about the individual. It has three components:
1. Self perception of the talents and abilities based on one's performance.
2. Self perceived motives and needs based on self-diagnosis and feedback
3. Self perceived attitudes and values based on interactions with the norms and values implicit in the organization. As per Schein there are 5 types of career anchors:

- Technical / functional competencies
- Managerial competencies

- Security
- Creativity
- Autonomy

Career Path Planning System

In general, the career development has two distinctive phases i.e. prior to acquiring qualification and after acquiring qualification. Career planning is primarily an HRD sub-system. It establishes the linkage between other sub-systems like manpower planning, job rotations, transfer, placement, training and performance appraisal. While implementing the career plan, the organization has to see that:

1. Policy of career planning is made explicit. Benchmarks are laid down.
2. Career path is a facility for growth and not a right for advancement.
3. Career path should be made known to the employee.
4. Career path is followed uniformly for all employees without bias.
5. Career path should be flexible to accommodate variation. For

effective implementation of career path, the organizations have to:

1. Define the career stages in relation to the organizational levels.
2. Identify the core jobs at each level
3. Define and spell out the criteria for each successive level.
4. Placement is the next career role.

SELF DEVELOPMENT

Organisations are required to bring about strategic changes involving business diversification, expansion and structural changes in response to emerging demands. Organisations are not able to bring total change of mindset of their people.

For creating learning organizations, the people in the organization have to be sensitized to the need for self-renewal. To achieve a lasting effect, the organizations have to concentrate on how the HR could be reoriented towards such self-renewal. Unless the individuals change, they would not be able to survive. The change in the organization comes only when the individuals sense that change is occurring and he has to take corrective steps to ensure that he does not become a misfit.

For self-development of the individual in the context of an organization, the under-noted aspects require consideration:

At individual level : motivation pattern, locus of control and power bases.

At inter-personal level : Interpersonal needs, Transactional Analysis

At group level : Being effective member in the work group

At Individual Level

Motivation pattern	Individuals have to be aware, what motivates them, what is his contribution to the group activities OR what kind of influence he is exerting. Such analysis can reveals that for job satisfaction he can look for those opportunities. It would facilitate creation of awareness about career anchor and then deciding what is the most suitable action for development and increasing effectiveness.
Locus of control	Concept given by Lefcourt and Levernson explains that individuals have beliefs about who is responsible for what happens in life. With some individuals there more external locus of control and with others there is internal locus of control. Such beliefs have impact on individual performance. A conscious effort by an individual as to who controls him, can reveal the areas of development. Specific strategies can be drawn by the individual to bring the desired orientation.
Power bases	As per Kotler, the power is a measure of person's potential to get others to do what he or she wants them to do, as well as avoid being forced to do what he or she does not want to do. A person become aware of the power he has and how much more is needed which is quite relevant. Perception of having and using power, empowers a person.

Interpersonal interactions:

There are a very large no. of situations in an organization, when people interact with each other and influence each other. Accordingly, people can acquire influencing styles.

According to Schutz, there are 3 basic interpersonal needs implied in interaction among people i.e. inclusion, control and affection.

Satisfactory relationship includes (a) a psychologically comfortable relationship with people on a dimension of initiating interaction and (b) a psychologically comfortable relationship with people with respect to eliciting the behaviour from others.

Transactional Analysis

Transactional Analysis (or TA) is the process of analyzing and understanding the beheviour of a human being. It helps in understanding the behaviour of the self and others, improve the inter-personal relationship and ensures effective communication.

The concept was developed by Eric Berne based on the concept of Freudian Psychology suggested by Sigmund Freud. He made the Freudian ego and superego simple by replacing with 3 ego states of human mind having no relationship with the age of a person. These ego states are:

Parent Nurturing and controlling and being critical

Adult Being logical, rational, having control over emotions, eagerness for problem solving, rational decision making

Child Being emotional, irrational, decision making normally not based on logic and rationale

People make basic assumptions about their own self-worth and also about the other people in the environment. Harris called these combinations as *Life Positions* which are described in the form of OKAYNESS.

PERONALITY TRAITS UNDER TRANSACTIONAL ANALYSIS

I am OK. You are OK (i.e. both have value)	I am OK. You are not OK (i.e. I have value and you do not have value)
I am not OK. You are OK (i.e. you have value but I do not have value)	I am not OK. You are not OK (i.e. neither person has value)

Based on the ego states, there are 4 personality traits of a person. The most appropriate under these is considered to be "I am OK. You are OK".

Self-awareness

Understanding self, helps in self-development. The concept of *Johari Window* by Luft and Ingham, explains what is meant by self-awareness. There are two dimensions (a) how much of one's behaviour is known to him (b) how much he feels others know him. These two dimension give 4 sections called (a) arena (b) blind (c) closed and (d) dark.

JOHARI WINDOW

	Known to self	Not known to self
Known to others	Arena (i.e. open space)	Blind
Not known to others	Closed	Dark

The size of arena is critical for improving effectiveness. More a person feels that other know him, more conducive the environment becomes and the better he is equipped, to face the challenges. Hence, Arena is required to be increased.

Emotional intelligence

As per Daniel Goleman link between IQ test scores and the achievements in life is dwarfed (dusted) by the

totality of other characteristics that one brings to life. These characteristics are called emotional intelligence (i.e. abilities such as being able to ¯motivate oneself and persist in the face of frustration, to control the impulse and dealy gratification, to regulate one's moods and keep away distress from swamping the ability to think. There are five *components* of emotional intelligence:

Self awareness : ability to recognize, understand, emotions and their effect on others.
Self regulation :ability to control disruptive impulse, to think before acting.
Motivation :Passion to work for reasons that go beyond money or status.
Empathy : Ability to understand emotions of others and treat people according to their
Social skills emotional reactions.
:Proficiency in managing relationships and building networks and ability to fund common ground and build rapport.

HUMAN IMPLICATIONS OF ORGANISATIONS

Human behaviour and individual differences

Human behaviour is a combination of originating and responding behaviour. It is the result of biological and psychological processes.

According to Kurt Lewin behaviour is a function of the person and environment around him.

The factors that influence the behaviour of an individual can be grouped as:

- Environmental factors — Economic, social, political.
- Personal factors — Age, sex, education, abilities, marital status and no. of dependents etc.
- Organisational factors — Physical facilities, organization structure and design, leadership, compensation and reward system etc.
- Psychological factors — Personality, perception, attitude, values, learning etc.

From the angle of an organization, the organization views the employees as the rational humans motivated by money. As a result, it adopts economic man and rational man approach.

However, economic motives alone may not influence the behaviour at the workplace. Other factors such as treatment, acknowledgement of their contribution etc. also affect the behaviour.

Employees behaviour at work

Employees behaviour at workplace plays important role in success of the organization. The people in an organization do not work in isolation and their role and performance is interdependent.

Assumptions about human behaviour at work:

1. There are difference between individuals.
2. Concept of a whole person
3. Behaviour of an individual is caused.
4. An individual has dignity.
5. Organisations are social systems.
6. There is mutuality of interest among organizational members.
7. Organisational behaviour is holistic.

There are certain commonalities in the persons such as persons like all other persons, like some other persons and like no persons.

Hence, the individuals have certain common characteristics.

There are several theories to explain the concept of personality. One dimension is in the form of Type A and Type B behaviour profiles.

A person with Type A behaviour is generally restless, impatient with a desire for quick achievement and perfectionism. Such managers in banks, usually keep their cabin untidy and it gives a messy appearance. His table may be full of papers and it may be difficult at times, to trace important papers on his table. He may be in the habit of blaming others.

On the other hand, Type B persons, are much more easy going, relaxed about time pressure, less competitive and more philosophical in nature. Such managers are systematic and methodical in their day to day work. They plan the work by differentiating as urgent and important.

EH Erikson identified 8 developmental stages in explaining the personality. These stages are:

Stage	Name
Stage-i	Trust vs mistrust
Stage-2	Autonomy vs shame & doubt
Stage-3	Initiative vs guilt
Stage-4	Industry vs inferiority
Stage-5	Identify vs role diffusion
Stage-6	Intimacy vs isolation
Stage-7	Generativity vs stagnation
Stage-8	Integrity vs despair

Personality Theories

There are certain common patterns and variable that determine the personality of the people. Experts have developed certain personality theories.

Psychoanalytical Theory	Based on Freudian concept of unconscious nature of personality. Human behaviour and motivation is outcome of psychoanalytic elements i.e. id, the ego and the super ego. Id is the foundation of unconscious. Ego is conscious in nature and relates the conscious urges to the outside world. Id demands immediate pleasure and Ego controls it. Super ego supports the Ego.
Trait Theory	There are many traits common to all but there are few traits that are unique to few. On the basis of traits, people are described as aggressive, loyal, pleasant, flexible, humorous, sentimental, impulsive etc.
Self-concept theory	Personality and behaviour is determined by the individual himself. We have our own image and our actions are consistent with such image (Carl Rogers). An employee with a self concept of high intelligence, independence and confidence may not look for such reinforcement techniques as monetary rewards.
Social learning theory	Personality development is more a result of social variables than biological factors. Much of human behaviour is learnt or modified by learning. Personality is the sum total of all that a person has learned.

Personality and Brain

Brain influences the personality. Such contribution of brain could be through Electrical simulation of the brain (ESB) and split brain psychology. It may be possible physically to manipulate personality through ESB.

The split brain (right vs left brain) psychology is closely related to ESB.

Left Hemisphere (controls right side of the body)	Right hemisphere (controls left side of the body)
Performs functions such as speech, logical (mathematical), linear (detailed) sequential, controlled, intellectual, dominant, active, analytic, reading, writing etc.	Performs functions such as special (musical), holistic, simultaneous, emotional, intuitive, creative, spiritual, facial recognition recognition of complex figures etc

Johan Hollands personality job fit theory :

Holland presents 6 personality types and proposes that satisfaction and dissatisfaction with the job

depends on how individuals successfully match their personality with their occupations. These 6 personality types include :

1.Realistic (shy, genuine, persistent stable, conforming, practical) — Farmers, mechanic, assembly line worker.

2.Investigative (analytical, original, curious, independent) — Biologist, economist, news reporter.

3.Social (sociable, friendly, cooperative, understanding) — social worker, teacher, counselor

4.Conventional (conforming, efficient, practical, unimaginative, bank teller, file clerk) accountant, corporate manager.

5.Enterprising (self-confident, ambitious, energetic, domineering) Lawyer, real-estate agent.

6.Artistic (imaginative, disorderly, idealistic, emotional, impractical)- painter, musician, writer.

Diversity

Race, ethnicity and gender are the more recognized forms of diversity. The diversity has implications for HR system such as disability, family background, age, life style and culture. These identity groups can affect the employee's attitude at workplace.

Previously, the organizations used to promote homogeneity which is called 'homogeneous reproduction'. But much similarity in the organization can be detrimental to long-term growth, renewal and ability to respond to important environmental changes such as dynamic market conditions, new technologies and ideas etc.

Modern employers encourage diversity at workplace. There are 3 predominant traditional HR approaches for managing diversity i.e.

(b) (a) **diversity enlargement** (this increases the representation of individuals of different ethnic and cultural backgrounds) **diversity sensitivity** (it acknowledges the existence of cultural distance and attempt to teach individual members about cultural differences via training) and

(c) **cultural audits** (it generally tries to determine what is blocking the progress of non-traditional employees).

Gender issues

Many jobs have preference for a particular gender both from employer's and employee's point of view due to physical, social, psychological and emotional considerations.

Jobs requiring physical strengths — men are preferred.

Jobs requiring hospitality — women are preferred.

Banking, teaching, healthcare etc. have all seen a good representation of women in India. To provide for equal remuneration, India has also passed The Equal Remuneration Act 1976. For providing against the vulnerability of women at workplace, Factories Act 1948 provides for special permission for requiring women to work at odd hours.

Supreme Court has also issued comprehensive directive against cases of exploitation, sexual harassment and discrimination at workplace.

Theories of Motivation and their practical implications

Motivation refers to a process beginning from the inner state of a person and ending with need fulfillment. When a student puts in hard work in studies, his motivation level is considered as high. When a worker shirks work, his motivation level is deemed to be low.

The word motivation is derived from a Latin word `movere' i.e. to move. As a behavioural concept, motivation is of great interest to the Managers in business organization.

There are various theories of motivation such as:

Theory	Description of the theory
Scientific management or Rational Economic View	FW Taylor contributed much to this theory. Theory states that: -Physical work could be scientifically studied to determine the optimal method of performing a job. -Workers can be made efficient by giving prescription. -Workers would be willing to accept these prescriptions, if paid on a differential piece work basis.

Human Relations Model	As per Elton Mayo, social contracts at workplace are important in addition to money. Workers can be motivated by acknowledging their social needs and making them feel useful and important.
Abraham Maslow's Need Hierarchy Theory	He identified five levels of needs: 1:**Physiological needs:** Food, rest, exercise, shelter etc. **2:Safety needs:** Protection against danger, threat, deprivation. **3:Social needs:** Need for belonging, for association, for acceptance, for giving and receiving friendship and love. **4:Ego/esteem needs:** Need For self confidence, for dependence, for achievement, for knowledge and need for status, recognition, appreciation. **5:Self-fulfillment or self-actualisation needs:** To realise one's own potentialities, to experience continued self-development, to be creative.
Frederick Herzberg's Two Factor Theory	It states that there are two sets of motivating factors i.e. hygiene or maintenance factors relating to job environment and other the motivators relating to contents of the job. **Motivational factors** include recognition, advancement, responsibility, achievement, possibility of growth & work itself. **Maintenance factors** include company policy and administration, technical supervision, salary, job security, personal life, working conditions, status, inter-personal relations with peers and supervisors.
Clayton Alderfer's ERG Theory	It is based on existence, relatedness and growth (ERG). People have needs in a hierarchy and these-needs determine the human behaviour. ERG theory has three levels of needs compared to 5 in case of Maslow. As per ERG theory, more than one-need may be operative at one point of time rather than only one need as per Maslow theory.
Achievement Motivation Theory	According to DC McCelland, there are three needs i.e. for achievement, for power and for affiliation.
Victor H Vroom's Expectancy Model	This theory is known by other names also *such* as instrumentality theory, path-goal theory, valence-instrumentality-expectancy theory. As per theory, motivation is determined by the nature of reward people expect to get as a result of their job. Man being rational tries to maximize his perceived value of such rewards. There are three elements in the model i.e. expectancy, instrumentality and valence (value a person assigns to the desired reward).
James Stacy Adams' Equity Theory	Theory proposes that motivation to act, develops after the person compares the inputs / outcomes with the identical ratio in comparison to the other person. Upon feeling inequity, the person is motivated to reduce it.
Lyman W Porter and Edward E Lawler—Performance satisfaction Model	It states that the motivation does not equal satisfaction and performance. These are all separate variables. Effort does not lead to performance directly. The reward that follows will determine the satisfaction.
Reinforcement Theory.	The consequences of an individual's behaviour in one situation influences that individual's behaviour in a similar situation.

Motivation and behaviour

Behaviour is generally influenced by a desire to achieve some goal and goal may be known to the individual or-it may not be known to him. Each activity is supported by motivation.

Motives - Individuals carry a set of inner motivations and drives that influence the way he behaves much more radically than he realizes. Motives are needs, wants, drives or impulses within the individual.

Goals - These are outside an individual. These are the hopes for rewards towards which the motives are directed.

Motivation To Work

There are several ways of motivating people at work such as money, appreciation, job enrichment, job rotation, participation.

Money	It is important motivator as money has the capability to meet several needs of a person. Maslow's physiological needs like food, clothing and shelter can be met by money. Money has a limited impact as motivator and it has diminishing returns.
Appreciation	An effective non-monetary benefit is the recognition and appreciation for good job. It satisfies self esteem need. It also has impact on other group members.
Job enrichment	A job is enriched when it is challenging and creative. It provides more decision making, planning and controlling experiences.
Job rotation	Shifting an employee from one job to another keeps his interest in the job intact. Besides, there is lot of learning opportunity in job rotation.
Participation	Participation of the employee in the management of an organization keeps the employee motivated.
Quality of work life	Adequate and fair compensation, safe and healthy environment, jobs aimed at developing and using employee's skills and abilities, integration of job career and family all contribute in improvement in quality of work life.

Role concept and analysis

Role refers to a set of expected behaviour patterns attributed to someone occupying a given position in an organization. Role and position are different concepts. Role is a position a person occupies in an organization and it is an obligational concept . Position is a relational and power related concept.
The concept of role widens the meaning of work and relationship of the employee with other significant persons in the system. There are few important aspect of role such as role stagnation, inter-role distance, role set conflict (which has various forms such as role ambiguity, role expectation conflict, role overload, role erosion, role inadequacy, personal inadequacy etc.)

Important aspect of Role

Role stagnation	When a person is promoted, he assumes a new role but if he fails in the new role, he experiences role stagnation, even though he occupies a new role. In turn this causes role stress. A senior clerk, when promoted as officer, may find himself in such a situation, at times.
Inter-role distance	If an individual occupies more than one role, there could be conflicts between the roles. A branch manager also performs the role of husband and father at home. When he is not able to give time to family, this creates stress.
Role set conflicts	Different people have different expectation from one role. There is possibility of incompatibility amongst expectation of others. It may then result into role ambiguity, role expectation conflict, role overload etc.
Role ambiguity	When the individual is not clear about the expectations from him about the role this is called role ambiguity. It may be in relation to activities, responsibilities, priorities or general expectations.
Role expectation conflict	When there are conflicting expectations or demand from a role, the role occupant experiences conflict and stress. These expectations may come from boss, customer,seers or subordinates.
Role overload	When a role occupants finds that there are too many expectations from the role. it may occur when the role occupant lacks power or where there are large variations in the expected output.
Role erosion .	Where the role occupants finds that certain functions that he is perform are being performed by someone else, having a different rol. It is individual's subjective feeling. In a small bank an additional post of general manager has been created. earlier there was one GM only. The existing GM may start feeling that there is role erosion.

Resource inadequacy	When the resources required for performance of a role are not adequacy, the role occupant may experience the resource inadequacy.
Personal inadequacy	When the role occupant finds that he does not have adequate skills, knowledge or experience to perform the role effectively.
Role isolation	When role occupant finds that certain roles are closer to him and other at a distance, the main criteria being the frequency and ease with which he could perform the role.

EMPLOYEES' FEED BACK AND REWARD SYSTEM

Progressive organizations make efforts to obtain regular feedback from the employee on various aspects of HRM. This is done by way of some satisfaction or climatic survey. The information is gathered both formally and informally about the attitude and satisfaction of employees. At formal level this is collected through well designed questionnaires, psychological, suggestion schemes etc. The informal information is gathered through discussions with the representatives of employee, observation of managers and superiors based on the behaviour pattern of the employees.

Thorough such surveys, the organization is able to understand as to how effectively, it is managing its people.

Feedback through climatic survey :

Under this, the organizations measure individuals' perception about the climate within the organization. The coverage of a typical climate survey can be as under:

1. Structure (employees' feeling about constraints on groups, rules, regulations, procedures, communication channel, delegation.)
2. Responsibility (employees' feeling about being your own boss, clarity of role)
3. - Reward (employees' feeling about being rewarded for good job, perception about reward and punishment system)
4. Risk (sense of riskiness and challenge in the job and in the organization)
5. Warmth (general feeling of fellowship, informal supporting culture)
6. Support (perception about helpfulness of managers)
7. Standards (perceived importance of implicit and explicit goals and performance standards)
8. Conflict (employees' feeling that the managers and others want to hear different opinion)
9. Identity (employees' feeling of belongingness to the organization and perceived value).

Reward and compensation

The wages as compensation is viewed as the main attraction to join or change a job. Compensation should be reasonable and justifiable to keep the employee happy and devoted in the organization. Basic aim of an individual is to earn satisfactory wages and perform well to be recognized for other financial and nonfinancial rewards.

Types of compensation ; Compensation refers to a monetary reward for the performance of the job plus other benefits. It include wages or salary, bonus, cash allowances, benefits such as accident, health insurance cover, employer' contribution to the retirement funds, provision for accommodation etc.

Type of position	**Compensation**
Managerial job (top, middle, junior)	Remuneration
Supervisory	Salary
Clerical or administrative	Salary
Unskilled, semi-skilled	Wages

Factors for deciding compensation : These factors could be:

(a) company objectives,
(b) employee market situation and
(c) internal and external pressures.

Compensation theories : According to 3rd pay commission, a_good compensation package covers factors like adequacy, societal considerations, supply and demand position, fairness, equal pay for equal work and

job evaluation.
Adequacy of wages : The committee on fair wages, pronounced certain wage concepts such as: Minimum wages,Living wages, Fair wages ,Need-based minimum wages.
Legal framework : The level of compensation theoretically gets decided by the socio-economic considerations. Administration, however, protects the workforce from irrationally low wages. In India, the Govt. has come out with following enactments:
The payment of wages Act 1936, The minimum wages Act 1948, The payment of bonus Act 1965 and The equal remuneration Act 1976.
Job evaluation: This is one of the important measures to determine the level of compensation package. It helps in distinguishing jobs in the level of complexity, skills required, the risk involved and link compensations accordingly. The objective of job evaluation are:
1. To determine the compensation rates.
2. To link pay with the requirement of the job
3. To provide for pay differential taking into account the skills, efforts, hazards required in each job.
4. To establish a compensation structure.

Process of job evaluation — It involves job analysis, job description and job specification. It is also important for manpower planning, performance appraisal.
Performance and rewards : From this angle, the compensation may be fixed, totally variable and mixed.
Fixed — Based on job analysis or market conditions or the collective bargaining power of the union, the compensation is fixed for various jobs. Fixed level creates low level of motivation.
Variable - Compensation is decided based on performance. This induces high level of performance.
Mixed — It tries to remove the drawbacks of both the variable and fixed compensation. A fixed level is fixed with the provision to give incentive for performance.

Practices in Indian Banking Industry

In Indian banking system, initially the structure of compensation was decided by the banks themselves. Later on, on formation of Unions and associations, the situation started taking different shapes. In the early 5os and 6os, the bank union contended that banks should pay according to capacity but bank management denied the same. The matter was referred to the Tribunal for adjudication.
The first such adjudication was in the form of Sastry Award followed by Desai Award.
Later on (since 1966) the system of Bipartite Settlement was put to practice. The settlement is binding on both the parties and is valid for 5 years.
Bank managements, of late have been of the view that the wage settlement should be bank wise.

PERFORMANCE MANAGEMENT

The basic objective of HRM is to create an environment, where the individual contributes his best to meet the corporate goals and gets satisfaction, out of what he does. Their performance is measured to examine their contribution and also for compensation.
Appraisal system :
Performance appraisal is an important tool both for the organization and the employee. It is a process by which the management finds out how effective it has been in hiring and placing the employees. It is an important tool to review employee performance, take corrective steps through training, interventions or placement decision, reward good performance and attempt to take the employee performance at a higher level.
The appraisal system may be formal or informal depending upon the requirements of the organization.
Objectives of the system:
According to McGregor, the performance appraisal plans meet 3 needs:
1. Judgemental for salary increases, transfers and promotions.
2. Developmental — telling an employee hoe is he doing and suggesting changes in his skills, attitude and behaviour.
3. Counselling by the superior.

The specific objective, the system should serve are:

1. To enable the organisation to maintain an inventory of the quality and skills of people and identify and meet their training needs_
2. To determine the performance linked increments and provide data for promotions and transfers.
3. To maintain individual and group development and fulfill their aspirations by sharing with them, their standard of observed performance and help them reach the benchmarked by skill upgradations programs.

Process of evaluation:

The process of evaluation has to take care of the following aspects:

- Organization sets up the performance standards, that should be clear, realistic and measurable.
- Standards are required to be conveyed to the employees.
- For measurement of performance, data is collected.
- Based on data/information; the performance is measured.
- Outcome of the appraisal is discussed with the employee emphasizing the strong points and counseling him on the weak points.
- Corrective steps are taken.

Appraisal methods

Each organization has to choose a method for performance appraisal, as it suits its requirement. There are two sets of methods i.e. traditional and modern methods.

Traditional methods	Modern methods
• Straight ranking method • Comparison method • Grading method • Graphic method • Forced choice method • Forced distribution method • Free form essay method • Group appraisal method.	• Assessment centre method • Management by objectives method • Human asset accounting method • Behaviourally anchored rating scale

The features of these methods are:

Method	Description
Straight ranking	Relative position is assessed and people are rated in order of merit and placed in a grouping,
Comparison	Employees are compared on certain selected factors like leadership, initiative etc. It is also called factor comparison method.
Grading	Certain features are considered for grading. Scales are decided on the basis of these grades which can be Outstanding (A), very good (B), average (C), below average(D)
Graphic or linear rating	Methods takes into account the employee characteristics and contribution. Rating is on a continuous scale.
Forced choice or distribution	Superior is made to make his choices to minimize the bias. Employee is rated on predetermined distribution scale.
Free form essay	Appraiser makes a free form, open-ended appraisal of the employee regarding job knowledge, attitude, development needs.
Group appraisal	Group of appraisers rate an employee who have some knowledge about employee's performance.
Assessment centre	It is a modern method. Employee's behaviour is assessed on the basis of performance of different activities such as group discussion, business games, in-basket exercise etc.
Management by objectives	It attempts to minimize the external controls and emphasizes on motivation levels of the employees. Objective of MBO is to change the behaviour and attitude for getting results.

Human asset accounting	Human assets, like other assets, are valuable. Money estimates are attached to the value of an organization's personnel and its external goodwill. Current value of the human assets is appraised by undertaking periodical measurement of two variables called key causal (i.e. management policies,strategies, skills) and intervening enterprise (loyalty, attitudes, motivation level).
Behaviourally anchored rating scale	Jobs are described through illustrations or by giving critical incidents of effective and ineffective performance. A scale is devised on the basis of thse incidents.

Management by objective method (MBO):

This system emphasizes on goal achievement rather than the method involved. The process is:

- Setting up of organisational goals.
- Goal setting is a joint process.
- Frequent reviews of performance through one to one meeting.
- Sharing of feedback in altering the course of action, if required.

Advantages — Involves participative approach in goal setting. (b) enhances motivational skills (c) creates an environment of competition within the organization for enhanced performance (d) provides objective appraisal method (e) early identification of problems.

Potential assessment:

The performance appraisals emphasizes the past performance and does not help much in making assessment about the potential performance. For this purpose, the organizations may make use of Potential Appraisal Report. The assessment centre method (of performance appraisal) used in conjuction with the performance appraisal system, can help in determining the potential.

Performance appraisal vs Confidential Report

Annual performance appraisal can also be carried as a confidential activity. This report is submitted to the controlling office. There is no transparency and the superior assumes greater importance and wields power. No feedback is given to the employee as to how he is performing. Hence, there is no developmental consideration.

Merits and demerits of Appraisal system

Merits	Demerits
• Reveals concern for performance • creates an environment_ of organization. • Provides feedback to the employees and steps are taken in time. • Raises general motivation level of the employees if	• There is halo effect i.e. rate an employee is or low. • Leniency or strictness tendency interferes with the appraisal and appraisal gets • Assigning average rating to all aspects of rating.

COUNSELLING

Among various facets of human relations, counselling is probably one of the oldest relationships. From ancient times till the development of modern management concepts, counselling as a technique has proved its worth time and again and has become an indispensable tool for the development of human beings.

Counselling refers to establishment of a relationship between tow persons where one assumes a superior role (by dint of his competence, capabilities and knowledge) as a counsellor and the other as a counsellee or client. Counselling is infusion of ideas, strength and showing direction to a person to behave or act in desired manner as expected of him.

Managerial counselling refers to a relationship between a superior and a subordinate and aims at paving the way for the development of subordinate as a human being notwithstanding the organisational needs and objectives. Here the supervisor help the subordinate to realise his potentials for development without resorting to the establishment of traditional relationship of counsellor and counsellee. This is done through an objective way of making the subordinate realise his position and trying to explore the goal jointly and heading towards it consciously. Here the supervisor intervenes in an objective way and thus helps the subordinate in a participative way.

Successful counselling:

a: Preparedness of the supervisor i.e. right and positive aptitude where he has to accept the fact that the whole exercise is going to be mutual between two normal people on a give and take basis. He must know the background, attitude, feeling and personality of the subordinate.

b: Tuning in with the subordinate i.e. accurate understanding of the subordinate so that the supervisor can really feel the pulse of the subordinate and can see the setting where the subordinate is standing as well as his view point. This is also known as empathy.

c: Acceptance of the subordinate as an individual and in totality.

d: He should be a good listener and patience to listen to subordinates carefully. He should encourage the subordinate to communicate as much as possible.

How to proceed : Dos and do-nots

a: Acquainting with the background.
b: Relaxed setting.
c: Facing the counsellee as a human being
d: Psychological rapport
e: Do not argue
f: Eliciting information.
g: Catching the contradictions and giving the feedback.
h: Identification of needs jointly.

The managerial counselling mentioned above revolves around the expectations of organisation from the human resources it engages. The gap between what the organisation wants its human resources to do and what they otherwise do is the area where, through various techniques-developments are possible and managerial counselling in this regard can play an important role as an effective technique.

Certain important information for questions on HRM (Common for all Chapters):

1 Attitude has emotional, informational, behaviourial dirnensions.
2 Attitude though difficult, but it can be changed.
3 One of the weapons to change the attitude is by arousing fear.
4 Attitude changes can be tried through influence of friends and peers, opinion leaders and co-opting people in the decision making process.
5 Career roles such as sponsor, colleague, apprentice and mentor can be arranged in the ascending order as sponsor, colleague, mentor and apprentice.
6 . In transaction analysis, the transaction is blocked When a transaction takes place between parent to parent.
7 An individual's personality has a combination of child, adult and parent ego status.
8 In transactional analysis "I am not OK, you are OK' stands for— I do not have value. You have value.
9 Every member of the group has to work out the task of the group, maintain the cohesiveness of the group and understand the decision making process of the group.
10 HR professionals must have concern for people and their development.
11 HR professionals must have ability to work as a team member
12 National Institute of Labour Management was started mainly for promotion and development of cordial relationship between employees and employers.
13 Howthrone Studies revealed that productivity depends on emotional state, relationship with colleagues, kind attention of the supervisors.
14 Application of IT to serve customers of a bank has tremendous potential.
15 The main task of knowledge management is to capture tacit knowledge of people for future use.
16 Andraqogy refers to adult learning.
17 Labour unrest and formation of unions was started because more emphasis was laid on work, there was :11,echoliicz.11 approach towards the workers, behaviour of the workers was totally ignored.
18 The central theme of Human Approach in Management is that the individuals are motivated by sense of achievement.

Module: D

Credit Management

SYLLABUS

Principles of Credit Management Credit Appraisal Analyzing Financial Performance - Relationship between items in Balance Sheet and Profit and Loss Account. Trend Analysis, Comparative Statement - Common size Statement, Preparation of projected Financial Statements. - Ratio analysis - Interpretation and analysis of different Ratios, Limitation of the use of ratios. Statement of Sources and Applications of Funds.
Structuring a Credit Proposal - Working Capital Concept and Management Appraisal techniques for different constituents - trade cycle - credit rating - Technical and economic feasibility studies - Credit Rating - Rating Methodology - Objectives and benefits of rating - Term Lending - Debt Service Coverage Ratio - Cash Flow Analysis - Cash Budget - Bill Finance - Deferred Payment Guarantee - Credit Scoring - Credit Delivery System - Documentation - Post sanction supervision, Control and monitoring of credit - Consortium finance, Multiple banking, Syndication of loans. Infrastructure financing.
Dealing with credit defaults, Stressed assets, Corporate Debt restructuring, SARFAESI, NPAs, recovery options, write-off. Disclosure of the list of defaulters: objectives and procedure. Appraisal methodology for different type of clients / products.

OVERVIEW CREDIT MANAGEMENT

Importance of Credit

Credit plays an important role in driving the national economy. It provides leverage to an entrepreneur to undertake a project larger than what he could have undertaken without availability of credit. This results in accelerated industrial production/services. It also enables individuals to first purchase/create assets and repay the loan from their future earnings. Credit enables a consumer to spend more than what he would have otherwise spent. The increased demand drives the producers to step up the production. Thus, adequate and cheap availability of credit propels the economy to higher growth trajectory. But, there is always a time lag between increase in demand and creation of supply to meet that demand. That is why excessive availability of credit, specially, for non-productive purposes, puts inflationary pressure of the economy.

Principles of Credit: (a) safety of funds (b) purpose (c) profitability (d) liquidity (e) security (f) risk spread

Types of Borrowers: A borrower can be (a) An individual (b) Sole proprietary firm (c) Partnership firm and joint ventures (d) Hindu undivided family (e) Companies (f) Statutory corporations (g) Trusts and co-operative Societies

The laws applicable to all these different kinds of borrowers and different. Individuals are governed by the Indian Contract Act, partnership firris by the Indian Partnership Act, Hindu undivided family by the customary laws pertaining to Hindus, companies by the Companies Act, statutory corporations by the Acts that created them, trusts by the Indian Trusts Act, Public Trusts Act, Religious and Charitable Endowments Act, Wakf Act and Co-operative Societies by the Co-operative Societies Act or the Societies Registration Act.

Types of Credit: Bank credit can be either fund-based or non fund-based.

1. Fund based credit: In fund-based credit, there is actual transfer of money from the bank to the borrower.
2. Non Fund based credit: In non fund based credit, there is no transfer of money, but the commitment by the bank on behalf of the client, may result in future transfer of money to the beneficiary of such a commitment. For example, a bank guarantee issued in favour of government departments (or any other beneficiary) on behalf of a contractor. If the beneficiary invokes the guarantee, the bank will have to remit the amount to it and the client, for whom guarantee was issued, will be liable to pay this amount to the bank. Thus, a non fund-based credit always has a possibility of getting converted into a fund-based credit. Other of non fund based credit are letters of credit, co-acceptance of bills, forward contracts, and derivatives.
3. Periodwise classification: The fund based credit can be short term credit or long term credit (term loan)
4. Purposewise classification: (a) working capital finance, (b) project finance, (c) export finance, (d) crop loan, etc.
5. Customerwise classification: Banks classify their credit portfolio on the type of the customers like, Corporate, retail, agriculture, international, institutional credit, etc.

Segmentwise classification: As per RBI guidelines, banks have to report their business, based on the geographical segments, as 'domestic' and 'international'. In addition, as per RBI guidelines, banks have adopted the following business segments, for public reporting purposes, from March 31, 2008:(a) Treasury (b) Corporate/Wholesale Banking (c) Retail Banking (d) Other Banking Business

1. Treasury: 'Treasury' for the purpose **of** Segment Reporting should include the entire investment portfolio.

2. Retail Banking: The Retail Banking .would include exposure which fulfill the following four criteria of orientation, product, granularity and low value of individual exposures for retail exposures laid down in Basel Committee on Banking Supervision document 'International Convergence of Capital Measurement and_ Capital Standards: A Revised Framework':

(a) Orientation Criterion: The exposure is to an individual person or persons or to a small business; Person under this clause would mean any legal person capable of entering into contracts and would include but not be restricted to individual, HUF, partnership firm, trust: private limited companies, public limited companies, co-operative societies, etc. Small business is one where the total annual turnover is less than Rs. 50 crore. The turnover criterion will be linked to the average of the last three years in the case of existing and projected turnover in the case of new entities.

(b) Product Criterion: The exposure takes the form of any of the following: revolving credits and lines of credit (including overdrafts), term loans and leases (e.g. instalment loans and leases, student and educational loans) and small business facilities and commitments.

(c) Granularity Criterion: No aggregate exposure to one counterpart should exceed 0.2 per cent of the overall retail portfolio, 'Aggregate exposure' means gross amount (i.e. not taking any benefit for credit risk mitigation into account) of all forms of debt exposures (e.g. loans or commitments) that individually satisfy the three other criteria. In addition, 'one counterpart' means one or several entities that may be considered as a single beneficiary (e.g. in the case of a small business that is affiliated to another small business, the limit would apply to the bank's aggregated exposure on both business).

(d) Low Value of Individual Exposures: The maximum aggregated retail exposure to one Counterpart should not exceed the absolute threshold limit of Rs.5 crore.

3. Corporate/Wholesale Banking: Wholesale Banking includes all advances to trusts, partnership firms, companies and statutory bodies, which are not included under 'Retail Banking'.

4. Other Banking Business: Other Banking Business' would include all other banking operations not covered under 'Treasury', Wholesale Banking' and 'Retail Banking' segments. It will also include all other residual operations such as banking transactions/activities.

COMPONENTS OF CREDIT MANAGEMENT

Loan Policy of the Bank: Each bank formulates its own loan policy and sanction of any credit proposal has to be within the framework of this policy. The formulation of loan policy is influenced by various factors like market conditions, policies of the competitors, bank's own SWOT analysis and, of course, the RBI guidelines. The loan policy normally contains guidelines about the following aspects:

(a) Exposure limits for single borrowers and groups

(b) Exposure limits for individual sectors like real estate, capital market, steel, cement, software etc. This is under constant watch of the bank and if bank's perception about any particular sector deteriorates, the exposure limits is reduced suitably and fresh sanctions of credit proposals, pertaining to that sector, are curtailed. In such cases, bank may even decide to exit some of the existing accounts by formulating suitable exit strategies. The loan policy also covers the thrust areas, low priority areas etc.

(c) Discretionary powers at various powers levels for sanctioning of credit proposals. Normally, the policy also lays down the various authorities for allowing over drawings/ad-hoc limits.

Appraisal: Before a lender agrees to give money to a borrower, as per his proposal, certain issues are checked which are given below:

(a) Trustworthiness of Borrower.
(b) Viability of the project/activity and the risks involved.
(c) Adequacy or otherwise of the amount of loan.
(d) Terms of repayment, interest rate etc.
(e) Prescription of covenants (terms and conditions) for effective monitoring of the project/activity.
(f) Need for Collateral security or personal guarantee.
(g) Method of creation of charge over primary/collateral security. Documents to be taken to enforce bank's claim in a court of law in case of default. ?

The complexity of this appraisal will depend on various factors like, amount involved, duration and purpose of loan, category of borrower, risks involved, security available, RBI guidelines etc. Thus, appraisal for a small crop loan or a vehicle loan will be different from that for an industrial project. For appraisal, the lender will normally depend on some or all of the following information/records, depending upon the uniqueness of each case.

(a) The background, credit history, market reports of the borrower.
(b) The financial track record of the borrowers as represented by the financial statements. Where these statements are not available, as in case of most of the individuals, the net worth and repayment capacity is judged by collecting details of assets and liabilities and sources of income.
(c) Techno-economic feasibility report of the activity proposed; The details required in this depend on the nature of activity being successful and bank getting back its principal and interest in time. Mostly, in case of industrial project only a detailed project report is prepared by the competent agency. In other cases, the viability is judged by the analysis of past track record, present financial position, source of income, expenditure and bank's own judgment.
(d) Securities available, their value and realisability.

Delivery: This relates to legal aspects of documentation and creation of charge over security. This also covers the method of delivery (like loan or cash in case of working capital limits) and procedure for disbursal of a term loan.

Control and Monitoring:This is necessary not only to ensure end use of the bank's funds also to ensure safety of it.

An efficient monitoring is in the interest of the borrowers as well, as the bank can provide timely help in case of unforeseen difficulties. It is very important for the bank as any delay in taking suitable action in cases of activity not being carried out as projected, reduces **the** chances and amount of recovery of bank's funds.

Rehabilitation and Recovery: Default is possible either due to genuine business problems or due to intentional (called willful) default. In the first case, the banks normally examine the feasibility of providing additional assistance/concessions/rephrasing etc. to help the enterprise to make its operations viable again. The widely known terms like rehabilitation of sick SSI units and Corporate Debt Restructuring (CDR) are part of this process. However, if rehabilitation is not considered feasible or, if the rehabilitation process does not yield the desired results, and in case of willful defaults, bank has to start the recovery process.

Credit Risk Management: Credit risk is major risk faced by a bank and it is very important that suitable policies are put in place to identify, measure and control this risk within acceptable limits. Refinance: This aspect of credit management assumes importance in times of tight liquidity position. There are elaborate norms for availing refinance from NABARD/SIDBI/ RBI in respect of certain priority sector advances. However, even if a bank avails of refinance for eligible advances, the risk remains with the bank. Therefore, this aspect does not affect bank's decision on a credit proposal.

ROLE OF RBI'S GUIDELINES IN BANK'S CREDIT MANAGEMENT: Following are some of the important RBI/Government guidelines/policies, which directly influence the credit management of a bank.

End Use of the Funds: It is the primary responsibility of banks to ensure proper end use of bank funds/ monitor the funds flow. Banks should ensure that drawals from cash credit/overdrafts accounts are strictly for the purpose for which the credit limits are sanctioned by them. There should be no diversion of working capital finance for acquisition of fixed assets, investments in associate companies/subsidiaries, and acquisition of shares, debentures, units of mutual funds, and other investments in the capital market.

PRIORITY SECTOR LENDING

RBI revised the priority sector lending guidelines with effect from April 23, 2015 on the basis of recommendations of an **Internal Working Group (IWG) headed by Ms Lily Vadera**. The salient features of the guidelines are as under:-

(i) Categories of the priority sector: Medium Enterprises, Social Infrastructure and Renewable Energy will form part of priority sector, in addition to the existing categories.

(ii) Agriculture: The distinction between direct and indirect agriculture is dispensed with.

(iii) Small and Marginal Farmers: A target of 8 percent of ANBC or CEOBE, whichever is higher, has been prescribed for Small and Marginal Farmers within agriculture.

(iv) Micro Enterprises: A target of 7.5% of ANBC or CEOBE, whichever is higher, has been prescribed for Micro Enterprises.

(v) Weaker Section: There is no change in the target of 10% of ANBC or CEOBE, whichever is higher.

(vi) Target for Foreign Banks: Foreign Banks with 20 branches and above already have priority sector targets and sub-targets for Agriculture and Weaker Sections, which are to be achieved by March 31, 2018. Foreign banks with less than 20 branches will move to Total Priority Sector Target of 40% of ANBC or CEOBE, whichever is higher, on par with other banks by 2019-20.

(vii) Bank loans to food and agro processing units will form part of Agriculture.

(viii) Export credit: Export credit upto 32% of ANBC or CEOBE, whichever is higher, will be eligible as part of priority sector for foreign banks with less than 20 branches. For other banks, the incremental export credit over corresponding date of the preceding year will be reckoned upto 2 percent of ANBC or CEOBE, whichever is higher.

(ix) The loan limits for housing loans and MFI loans qualifying under priority sector have been revised.

(x) The priority sector non-achievement will be assessed on quarterly average basis at the end of the respective year from 2016-17 onwards, instead of annual basis as at present.

(xi) The revised guidelines are operational with effect from 23 April 2015.

Categories under priority sector

1. Agriculture
2. Micro, Small and Medium Enterprises
3. Export Credit

4. Education
5. Housing
6. Social Infrastructure
7. Renewable Energy
8. Others

Targets /Sub-targets for Priority sector Domestic scheduled commercial banks and Foreign banks with 20 branches and above

Total Priority Sector: 40% of Adjusted Net Bank Credit (ANBC) or Credit Equivalent Amount of Off-Balance Sheet Exposure (CEOBE), whichever is higher.

Agriculture: 18% of ANBC or CEOBE, whichever is higher. Small and Marginal Farmers: Within the 18% target for agriculture, target for Small and Marginal Farmers will be 8% of ANBC or CEOBE, whichever is higher. This target to be achieved in a phased manner i.e., 7% by March 2016 and 8% by March 2017.

Micro Enterprises: 7.5% of ANBC or CEOBE, whichever is higher to be achieved in a phased manner i.e. 7% by March 2016 and 7.5% by March 2017.

Advances to Weaker Sections: 10% of ANBC or CEOBE, whichever is higher.

Achievement of Targets by foreign banks: Foreign banks with 20 branches and above have to achieve the Total Priority Sector Target, Agriculture Target, Weaker Section Target within a maximum period of five years starting from April 1, 2013 and ending on March 31, 2018. The sub-target for Small and Marginal farmers and for Micro enterprises would be made applicable post 2018 after a review in 2017.

Foreign banks with less than 20 branches

Total Priority Sector: 40% of ANBC or CEOBE, whichever is higher to be achieved in a phased manner by March 2012 – (32% by 2015-16, 34% by 2016-17, 36% by 2017-18, 38% by 2018-19, 40% by 2019-20. The additional priority sector lending target of 2% of ANBC each year from 2016-17 to 2019-20 to be achieved by lending to sectors other than exports. The sub targets, if to be made applicable post 2020, would be decided in due course.

Computation of Adjusted Net Bank Credit (ANBC)

Bank Credit in India [Item No.VI of Form 'A' under Section 42 (2) of the RBI Act, 1934].	**I**
Bills Rediscounted with RBI and other approved Financial Institutions	**II**
Net Bank Credit (NBC) - For the purpose of priority sector computation only	**III (I-II)**
Bonds/debentures in Non-SLR categories under HTM category+ other investments eligible to be treated as priority sector +Outstanding Deposits under RIDF and other eligible funds with NABARD, NHB and SIDBI on account of priority sector shortfall + outstanding PSLCs	**IV**
Eligible amount for exemptions on issuance of long-term bonds for infrastructure and affordable housing	**V**
Eligible advances extended in India against the incremental FCNR (B)/NRE deposits, qualifying for exemption from CRR/SLR requirements.	**VI**
ANBC	**III+IV-VVI**

For calculation of Credit Equivalent Amount of Off-Balance Sheet Exposures, banks to follow Master Circular on Exposure Norms.

Description of the eligible categories under PS : **1. Agriculture**

There will not be any distinction between direct and indirect agriculture. Lending to agriculture sector has been redefined to include (i) Farm Credit (which will include short-term crop loans and medium/long-term credit to farmers) (ii) Agriculture Infrastructure and (iii) Ancillary Activities.

1.1 Farm credit

A. Loans to individual farmers [including Self Help Groups (SHGs) or Joint Liability Groups (JLGs), i.e. groups of individual farmers, provided banks maintain disaggregated data of such loans], directly engaged in Agriculture and Allied Activities, viz., dairy, fishery, animal husbandry, poultry, bee-keeping and sericulture. This will include:

2. 1. Crop loans to farmers, including traditional/ nontraditional plantations and horticulture, and allied activities. Medium and long-term loans to farmers for agriculture and allied activities (e.g. purchase of agricultural implements and machinery, loans for irrigation and other developmental activities undertaken in the farm, and developmental loans for

allied activities.)

3. Loans to farmers for pre and post-harvest activities, viz., spraying, weeding, harvesting, sorting, grading and transporting of their own farm produce.
4. Loans to farmers up to Rs 50 lakh against pledge/hypothecation of agricultural produce (including warehouse receipts) for a period not exceeding 12 months.
5. Loans to distressed farmers indebted to non-institutional lenders.
6. Loans to farmers under the Kisan Credit Card Scheme.
7. Loans to small and marginal farmers for purchase of land for agricultural purposes.

B. Loans to corporate farmers, farmers' producer organizations/companies of individual farmers, partnership firms and co-operatives of farmers directly engaged in Agriculture and Allied Activities, viz., dairy, fishery, animal husbandry, poultry, bee-keeping and sericulture up to an aggregate limit of Rs 2 crore per borrower. This will include loans as per categories listed at A(i, ii, iii and iv)

1.2. Agriculture infrastructure

1. Loans for construction of storage facilities (warehouses, market yards, godowns and silos) including cold storage units/ cold storage chains designed to store agriculture produce/products, irrespective of their location.
2. Soil conservation and watershed development.
3. Plant tissue culture and agri-biotechnology, seed production, production of bio-pesticides, bio-fertilizer, and vermi composting.

For the above loans, an aggregate sanctioned limit of Rs 100 crore per borrower from the banking system, will apply.

1.3.Ancillary activities

1. Loans up to Rs 5 crore to co-operative societies of farmers for disposing of the produce of members.
2. Loans for setting up of Agriclinics and Agribusiness Centres.
3. Loans for Food and Agro-processing up to an aggregate sanctioned limit of Rs 100 crore per borrower from the banking system.
4. Bank loans to Primary Agricultural Credit Societies (PACS), Farmers' Service Societies (FSS) and Large-sized Adivasi Multi-Purpose Societies (LAMPS) for on-lending to agriculture.
5. Loans sanctioned by banks to MFIs for on-lending to agriculture sector as per the conditions specified in paragraph IX of this circular
6. Outstanding deposits under RIDF and other eligible funds with NABARD on account of priority sector shortfall.

For computing 7% / 8% target, Small and Marginal Farmers will include the following:-

1. Farmers with landholding of up to 1 hectare are considered as Marginal Farmers. Farmers with a landholding of more than 1 hectare and upto 2 hectares are considered as Small Farmers.
2. Landless agricultural labourers, tenant farmers, oral lessees and share-croppers.
3. Loans to Self Help Groups (SHGs) or Joint Liability Groups (JLGs), i.e. groups of individual Small and Marginal farmers directly engaged in Agriculture and Allied Activities, provided banks maintain disaggregated data of such loans.
4. Loans to farmers' producer companies of individual farmers, and co-operatives of farmers directly engaged in Agriculture and Allied Activities, where the membership of Small and Marginal Farmers is not less than 75 per cent by number and whose land-holding share is also not less than 75 per cent of the total landholding.

2. Micro, Small and Medium Enterprises (MSMEs)

2.1. The limits for investment in plant and machinery/equipment for manufacturing / service enterprise, as notified by Ministry of Micro, Small and Medium Enterprises, vide S.O.1642(E) dated September 9, 2006 are as under:-

Manufacturing Sector	
Enterprises	Investment in plant and machinery
Micro Enterprises	Does not exceed twenty five lakh rupees
Small Enterprises	More than twenty five lakh rupees but does not exceed five crore rupees
Medium Enterprises	More than five crore rupees but does not exceed ten crore rupees
Service Sector	

Enterprises	Investment in equipment
Micro Enterprises	Does not exceed ten lakh rupees
Small Enterprises	More than ten lakh rupees but does not exceed two crore rupees
Medium Enterprises	More than two crore rupees but does not exceed five crore rupees

Eligibility of enterprises for PS classification:

Manufacturing Enterprises: Bank loan to Micro, Small and Medium Enterprises irrespective of amount of loan.

Service Enterprises: Bank loans up to Rs 5 crore per unit to Micro and Small Enterprises and Rs 10 crore to Medium Enterprises engaged in providing or rendering of services.

Khadi and Village Industries Sector (KVI): All loans to units in the KVI sector will be eligible for classification as Micro enterprise under the sub-target of 7 percent /7.5 percent prescribed for Micro Enterprises under priority sector.

Other Finance to MSMEs

1. Loans to entities involved in assisting the decentralized sector in the supply of inputs to and marketing of outputs of artisans, village and cottage industries.
2. Loans to co-operatives of producers in the decentralized sector viz. artisans, village and cottage industries.
3. Loans sanctioned by banks to MFIs for on-lending to MSME sector
4. Credit outstanding under General Credit Cards (including Artisan Credit Card, Laghu Udyami Card, Swarojgar Credit Card, and Weaver's Card etc. catering to the non-farm entrepreneurial credit needs of individuals).
5. Outstanding deposits with SIDBI on account of priority sector shortfall.

Sub categorization of Micro enterprises: The earlier sub-categorization within the definition of micro enterprises (i.e. investment up to Rs 10 lac in plant and machinery and up to Rs 4 lakh in equipment) has been dispensed with.

Continuation of MSME status: The MSME units will continue to enjoy the priority sector lending status up to three years after they grow out of the MSME category concerned.

3. Export Credit

Domestic banks: Incremental export credit over corresponding date of the preceding year, up to 2% of ANBC or CEOBE, whichever is higher, effective from April 1, 2015 subject to a sanctioned limit of □25 crore per borrower to units having turnover of up to □100 crore. For foreign banks with 20 or more branches in India, this will be effective from April 1, 2017.

Foreign banks with less than 20 branches: Export credit will be allowed up to 32 percent of ANBC or CEOBE, whichever is higher.

4. Education

Loans to individuals for educational purposes including vocational courses upto Rs 10 lakh irrespective of the sanctioned amount will be considered as eligible for priority sector. Now even for education abroad loans up to Rs 10 lakh will be eligible for coverage under priority sector.

5. Housing

1. Loan for purchase/construction of a dwelling unit per family: up to Rs 28 lakh in metropolitan centres (with population of ten lakh and above) and loans up to Rs 20 lakh in other centres provided the overall cost of the dwelling unit in the metropolitan centre and at other centres should not exceed Rs 35 lakh and Rs 25 lakh respectively. The housing loans to banks' own employees will be excluded. Housing loans backed by long term bonds which are exempt from ANBC should either be included as loans to individuals up to Rs 28 lakh in metropolitan centres and Rs 20 lakh in other centres under priority sector or take benefit of exemption from ANBC, but not both.
2. Loans for repairs to damaged dwelling units: up to Rs 5 lakh in metropolitan centres and up to Rs 2 lakh in other centres.
3. Bank loans to any governmental agency for construction of dwelling units or for slum clearance and rehabilitation of slum dwellers subject to a ceiling of Rs 10 lakh per dwelling unit.
4. Housing projects for EWS or LIG: Loans for housing projects exclusively for the purpose of construction of houses for economically weaker sections and low income groups, the total cost of which does not exceed Rs 10 lakh per dwelling unit. For the purpose of identifying the economically weaker sections and low income groups, the family income limit of Rs 2 lakh per annum, irrespective of the location, is prescribed.

Bank loans to Housing Finance Companies (HFCs), approved by NHB for their refinance, for on-lending for the purpose of purchase/construction/reconstruction of individual dwelling units or for slum clearance and rehabilitation of slum dwellers, subject to an aggregate loan limit of Rs 10 lakh per borrower. The eligibility under priority sector loans to HFCs is restricted to 5% of the individual bank's total priority sector lending. The maturity of bank loans should be co-terminus with average maturity of loans extended by HFCs.

5. Outstanding deposits with NHB on account of priority sector shortfall.

6. Social infrastructure

Bank loans up to a limit of Rs 5 crore per borrower for building social infrastructure for activities namely schools, health care facilities, drinking water facilities and sanitation facilities in Tier II to Tier VI centres.

7. Renewable Energy

Bank loans up to a limit of Rs 15 crore to borrowers for purposes like solar based power generators, biomass based power generators, wind mills, micro-hydel plants and for non-conventional energy based public utilities viz. street lighting systems, and remote village electrification. For individual households, the loan limit will be Rs 10 lakh per borrower.

8. Others

1. Loans not exceeding Rs 50,000/- per borrower provided directly by banks to individuals and their SHG/JLG, provided the individual borrower's household annual income in rural areas does not exceed Rs 100,000/- and for non-rural areas it does not exceed Rs 1,60,000/-.
2. Loans to distressed persons [other than farmers) not exceeding Rs 100,000/- per borrower to prepay their debt to non-institutional lenders.
3. Overdrafts extended by banks upto Rs 5,000/- under Pradhan Mantri Jan-DhanYojana (PMJDY) accounts provided the borrowers household annual income does not exceed Rs 100,000/- for rural areas and Rs 1,60,000/- for non-rural areas.
4. Loans sanctioned to State Sponsored Organisations for Scheduled Castes/ Scheduled Tribes for the specific purpose of purchase and supply of inputs and/or the marketing of the outputs of the beneficiaries of these organisations.

IV. Weaker Sections

1. Small and Marginal Farmers
2. Artisans, village and cottage industries where individual credit limits do not exceed Rs 1 lakh
3. Beneficiaries under Government Sponsored Schemes such as National Rural Livelihoods Mission (NRLM), National Urban Livelihood Mission (NULM) and Self Employment Scheme for Rehabilitation of Manual Scavengers (SRMS)
4. Scheduled Castes and Scheduled Tribes
5. Beneficiaries of Differential Rate of Interest (DRI) scheme
6. Self Help Groups
7. Distressed farmers indebted to non-institutional lenders
8. Distressed persons other than farmers, with loan amount not exceeding Rs 1 lakh per borrower to prepay their debt to non-institutional lenders
9. Individual women beneficiaries up to Rs 1 lakh per borrower
10. Persons with disabilities
11. Overdrafts upto Rs 5,000/- under Pradhan Mantri JanDhanYojana (PMJDY) accounts, provided the borrowers' household annual income does not exceed Rs 100,000/- for rural areas and Rs 1,60,000/- for non-rural areas
12. Minority communities as may be notified by Government of India from time to time

Investments eligible for classification as PS

1. Investments by banks in securitised assets: (i) Investments by banks in securitised assets, representing loans to various categories of priority sector, except 'others' category, provided (a) the securitised assets are originated by banks and financial institutions and are eligible to be classified as priority sector advances prior to securitization; (b) the all inclusive interest charged to the ultimate borrower by the originating entity should not exceed the Base Rate of the investing bank plus 8% p.a.

(ii) Investments by banks in securitised assets originated by NBFCs, where the underlying assets are loans against gold jewellery, are not eligible for priority sector status.

2. Transfer of Assets through Direct Assignment /Outright purchases:

(i) Assignments/Outright purchases of pool of assets by banks representing loans under various categories of priority sector, except the 'others' category, provided: (a) the assets are originated by banks and financial institutions which are eligible to be classified as priority sector advances; (b) the eligible loan assets so purchased should not be

disposed of other than by way of repayment; (c) the all inclusive interest charged to the ultimate borrower by the originating entity should not exceed the Base Rate of the purchasing bank plus 8% p.a.

(ii) When the banks undertake outright purchase of loan assets from banks/ financial institutions to be classified under priority sector, they must report the nominal amount actually disbursed to end priority sector borrowers and not the premium embedded amount paid to the sellers.

(iii) Purchase/ assignment/investment transactions undertaken by banks with NBFCs, where the underlying assets are loans against gold jewellery, are not eligible for priority sector status.

3. Inter Bank Participation Certificates: (IBPCs) bought by banks, on a risk sharing basis,

4. Priority Sector Lending Certificates: The outstanding priority sector lending certificates bought by the banks.

Monitoring of Priority Sector Lending targets

To ensure continuous flow of credit to priority sector, the monitoring will be on 'quarterly' basis instead of annual basis. The data on priority sector advances have to be furnished by banks at quarterly and annual intervals.

Non-achievement of Priority Sector targets

Scheduled Commercial Banks having any shortfall in lending to priority sector shall be allocated amounts for contribution to the Rural Infrastructure Development Fund (RIDF) established with NABARD and other Funds with NABARD/NHB/SIDBI, as decided by RBI from time to time. For the year 2015-16, the shortfall in achieving priority sector target/sub-targets will be assessed based on the position as on March 31, 2016. From financial year 2016-17 onwards, the achievement will be arrived at the end of financial year based on the average of priority sector target /sub-target achievement as at the end of each quarter. The interest rates on banks' contribution to RIDF or any other Funds, tenure of deposits, etc. shall be fixed by RBI. The misclassifications reported by the Reserve Bank's Department of Banking Supervision would be adjusted/ reduced from the achievement of that year, to which the amount of declassification/ misclassification pertains, for allocation to various funds in subsequent years. Non-achievement of priority sector targets and sub-targets will be taken into account while granting regulatory clearances/approvals for various purposes

Common guidelines for priority sector loans

1. Rate of interest: As per directives issued by RBI.
2. Service charges: No loan related and adhoc service charges/inspection charges on priority sector loans up to Rs 25,000.
3. Receipt, Sanction/Rejection/Disbursement Register: A register/ electronic record should be maintained by the bank, wherein the date of receipt, sanction/rejection/disbursement with reasons thereof, etc., should be recorded.
4. Issue of Acknowledgement of Loan Applications: Banks should provide acknowledgement for loan applications received under priority sector loans. Bank Boards should prescribe a time limit within which the bank communicates its decision in writing to the applicants.

Bank loans to MFIs for on-lending

(a) Bank credit to MFIs extended for on-lending to individuals and also to members of SHGs / JLGs will be eligible for categorisation as priority sector advance under respective categories viz., Agriculture, Micro, Small and Medium Enterprises, and 'Others', as indirect finance, provided not less than 85% of total assets of MFI (other than cash, balances with banks and financial institutions, government securities and money market instruments) are in the nature of "qualifying assets". Aggregate amount of loan, extended for income generating activity, should be not less than 50% of the total loans given by MFIs.

(b) A "qualifying asset" shall mean a loan disbursed by MFI, which satisfies the following criteria:

(i) The loan is to be extended to a borrower whose household annual income in rural areas does not exceed Rs 1,00,000/- while for non-rural areas it should not exceed Rs 1,60,000/-.

(ii) Loan does not exceed Rs 60,000/- in the first cycle and Rs 100,000/- in the subsequent cycles.

(iii) Total indebtedness of the borrower does not exceed Rs 1,00,000/-.

(iv) Tenure of loan is not less than 24 months when loan amount exceeds Rs 15,000/- with right to borrower of prepayment without penalty.

(v) The loan is without collateral.

(vi) Loan is repayable by weekly, fortnightly or monthly installments at the choice of the borrower.

(c) Caps on margin and interest rate

(i) Margin cap: The margin cap should not exceed 10% for MFIs having loan portfolio exceeding Rs 100 crore and 12% for others. The interest cost is to be calculated on average fortnightly balances of outstanding

borrowings and interest income is to be calculated on average fortnightly balances of outstanding loan portfolio of qualifying assets.

(ii) Interest cap on individual loans: Interest rate on individual loans will be the average Base Rate of five largest commercial banks by assets multiplied by 2.75% or cost of funds plus margin cap, whichever is less. The average of the Base Rate shall be advised by Reserve Bank of India.

(iii) Components are to be included in pricing of loans viz., (a) a processing fee not exceeding 1% of the gross loan amount, (b) interest charge and (c) the insurance premium.

The processing fee is not to be included in the margin cap or the interest cap. Only the actual cost of insurance i.e. actual cost of group insurance for life, health and livestock for borrower and spouse can be recovered; administrative charges may be recovered as per IRDA guidelines. There should not be any penalty for delayed payment. No Security Deposit/ Margin are to be taken.

Terms and Conditions for Priority Sector Advances

1. Loans up to Rs 25,000 in PS there is no margin, no collateral security, no penal interest on advance, no processing fees and no inspection charge.
2. Loan more than Rs 25,000, the margin will be from 15% to 25%. For Loans beyond Rs 25,000, bank can ask for TPG/collateral security or both.
3. Loan application disposal norms : As decided by Bank's Board of Directors
4.

COLLATERAL SECURITY

For agriculture: NIL In case of:	Up to Rs.100000. Up to Rs.3 lac in case of recovery tie-up
Other priority sector	Up to Rs.25000 nil
Micro & Small Enterprises: -normal accounts -good track record a/c -accounts guaranteed under CGF guarantee	Not to be insisted upon: Up to Rs.10 lac Up to Rs.25 lac up to Rs.100 lac Up to Rs.5 lac — nil
Agro clinics & business centres	
SGSY: -Individual up to Rs.100000 -Group up to Rs. 10 lac	Not to be obtained up to this amount
SISRY	Not to be obtained
Education loan up to Rs.7.50 lac	Not to be obtained up to this amount.

PROCESSING/INSPECTION FEE, SERVICE CHARGE, PENAL INIT IN PRIORITY SECTOR ADVANCES

1.For loans up to Rs.25000 No charges

2.For loans above Rs.25000 Bank discretion

EXPOSURE NORMS

1. introduction: Exposure Norms are applicable to all scheduled commercial banks, excluding Regional Rural Banks. These have been prescribed as a prudential measure aimed at better risk management and avoidance of concentration of credit risks. Exposure Norms have been provided as ceiling on exposure to individuals or Groups; capital market exposures; unsecured exposure and other related items details of which are given below:

2. Credit Exposures to Individual/Group Borrowers:

a) Ceiling (i) The exposure ceiling limits would be 15 percent of capital funds in case of a single borrower and 40 percent of capital funds in the case of a borrower group. (ii) Credit exposure to a single borrower may exceed the exposure norm of 15 percent of the bank's capital funds by an additional 5 percent (i.e. up to 20 percent) and credit exposure to borrowers belonging to a group may exceed the exposure norm of 40 percent of the bank's capital funds by an additional 10 percent (i.e., up to 50 percent), provided the additional credit exposures are on account of extension of credit to infrastructure projects. (iii) In addition to the exposure permitted above, banks may, in exceptional circumstances, with the approval of their Boards, consider enhancement of the exposure to a borrower

(single as well as group) up to a further 5 percent of capital funds subject to the borrower consenting to the banks making appropriate disclosures in their Annual Reports. (iv) With effect from May 29, 2008, the exposure limit in respect of single borrower has been raised to twenty five percent of the capital funds, only in respect of Oil Companies who have been issued Oil Bonds (which do not have SLR status) by Government of India. In addition to this, banks may in exceptional circumstances, consider enhancement of the exposure to the Oil Companies up to a further 5 percent of capital funds. (v) The bank should make appropriate disclosures in the 'Notes on account' to the annual financial statements in respect of the exposures where the bank had exceeded the prudential exposure limits during the year pi) The exposure limits will also be applicable to lending under consortium arrangements (vii) Bills purchased / discounted I negotiated under LC (where the payment to the beneficiary is not made 'under reserve') will be treated as an exposure on the LC issuing bank and not on the borrower. In the case of negotiations ' under reserve' the exposure should be treated as on the borrower.

(b) Exposures to NBFCs : The exposure (both lending and investment, including off balance sheet exposures) of a bank to a single NBFC / NBFC-AFC (Asset Financing Companies) should not exceed 10% / 15% respectively, of the bank's capital funds as per its last audited balance sheet. Banks may, however, assume exposures on a single NBFC / NBFC-AFC up to 15%120% respectively, of their capital funds provided the exposure in excess of 10%/15% respectively, is on account of funds on-lent by the NBFC / NBFC-AFC to the infrastructure sector. Further, banks may also consider fixing internal limits for their aggregate exposure to all NBFCs put together. Infusion of capital funds after the published balance sheet date may also be taken into account for the purpose of reckoning capital funds. Banks should obtain an external auditor's certificate on completion of the augmentation of capital and submit the same to the Reserve Bank of India (Department of Banking Supervision) before reckoning the additions to capital funds.

(c) Exemptions: Following types of credit will not be reckoned for exposure norms: (i) Existing/additional credit facilities (including funding of interest and irregularities) granted to weak/sick industrial units under rehabilitation packages. (ii) Food credit: Borrowers, to whom limits are allocated directly by the Reserve Bank for food credit, will be exempt from the ceiling. (iii) Where principal and interest are fully guaranteed by the Government of India (iv) Loans and advances (both funded and non-funded facilities) granted against the security of a bank's own term deposits to the extent that the bank has a specific lien on such deposits. (v) Exposure on NABARD; However, there is no exemption from the prohibitions relating to investments in unrated non-SLR securities. Definitions: For the purpose of exposure norms, exposure, capital fund, Group and Infrastructure have been defined as under:

(d) Exposure: (a) Exposure shall include credit exposure (funded and non-funded credit limits) and investment exposure (including underwriting and similar commitments). The sanctioned limits or outstandings, whichever are higher, shall be reckoned for arriving at the exposure limit. However, in the case of fully drawn term loans, where there is no scope for re-drawal of any portion of the sanctioned limit, banks may reckon the outstanding as the exposure. (b) Credit exposure comprises of the following elements (i) all types of funded and non-funded credit limits. (ii) facilities extended by way of equipment leasing, hire purchase finance and factoring services. (c) Investment exposure comprises of the following elements: (i)investments in shares and debentures of companies (ii)investment in PSU bonds (c)investments in Commercial Papers (CPs). (d) Banks' I Fls' investments in debentures/ bonds / security receipts / pass-through certificates (PTCs) issued by a SC / RC as compensation consequent upon sale of financial assets will constitute exposure on the SC I RC. In view of the extraordinary nature of the event, banks / Fls will be allowed, in the initial years, to exceed the prudential exposure ceiling on a case-to-case basis. (e) The investment made by the banks in bonds and debentures of corporates which are guaranteed by a Public Financial Institutions (PFI) (as per list given by RBI) will be treated as an exposure by the bank on the PFI and not on the corporate. (f) Guarantees issued by the PFI to the bonds of corporates will be treated as an exposure by the PFI to the corporates to the extent of 50 percent, being a non-fund facility, whereas the exposure of the bank on the PFI guaranteeing the corporate bond will be 100 percent. The PFI before guaranteeing the bonds/debentures should, however, take into account the overall exposure of the guaranteed unit to the financial system.

(e) Capital Funds: Capital funds for the purpose will comprise of Tier I and Tier II capital as defined under capital adequacy standards and as per the published accounts as on March 31 of the previous year. However, the 'infusion of capital under Tier I and Tier II, either through domestic or overseas issue (in the case of branches of foreign banks operating in India, capital funds received by them from their Head Office), after the published balance sheet date will also be taken into account for determining the exposure ceiling. Other accretions to capital funds by way of quarterly profits etc. would not be eligible to be reckoned for determining the exposure ceiling. Banks are also prohibited from taking exposure in excess of the ceiling

in anticipation of infusion of capital at a future date.
(p Group: (a) The concept of 'Group' and the task of identification of the borrowers belonging to specific industrial groups is left to the perception of the banks/financial institutions. However, the guiding principle will be commonality of management and effective control. In so far as public sector undertakings are concerned, only single borrower exposure limit would be applicable. (b) In the case of a split in the group, if the split is formalized, the splinter groups will be regarded as separate groups. If banks and financial institutions have doubts about the bona fides of the split, a reference may be made to RBI for its final view in the matter to preclude the possibility of a split being engineered in order to prevent coverage under the Group Approach.

INTEREST RATES ON LENDING

An objective of financial sector reform has been to ensure that the financial repression inherent in administered interest rates is removed. Accordingly, in the context of granting greater functional autonomy to banks, effective October 18, 1994, RBI decided to free the lending rates of scheduled commercial banks for credit limits of over Rs. 2 lakh; for loans up to Rs. 2 lakh, it was decided that it was necessary to continue to protect these borrowers by prescribing the lending rates and accordingly it was prescribed that for loans up to and inclusive of Rs.2 lakh, the fending rates of banks should not exceed the BPLR of the

respective banks. For credit limits of over Rs.2 lakh, the prescription of minimum lending rate was abolished and banks were given the freedom to fix the lending rates for such credit limits subject to BPLR and spread guidelines. Banks were required to obtain the approval of their respective Boards for the Benchmark Prime Lending Rate (BPLR), which would be the reference rate for credit limits of over Rs.2 lakh. Each bank's BPLR has to be declared and be made uniformly applicable at all branches.

The BPLR system, introduced in 2003, fell short of its original objective of bringing transparency to lending rates. This was mainly because under the BPLR system, banks could lend below BPLR. For the same reason, it was also difficult to assess the transmission of policy rates of the Reserve Bank to lending rates of banks. Accordingly, based on the recommendations of the Working Group on Benchmark Prime Lending Rate which submitted its report in October 2009, banks have been advised to switch over to the system of Base Rate with effect from July 1, 2010. The Base Rate system is aimed at enhancing transparency in lending rates of banks and enabling better assessment of transmission of monetary policy.

Base Rate

1. The Base Rate system will replace the BPLR system with effect from July 1, 2010. For loans sanctioned up to June 30, 2010, BPLR will be applicable. However, for those loans sanctioned up toJune 30, 2010 which come up for renewal from July 1, 2010 onwards, Base Rate would be applicable.
2. Base Rate shall include all those elements of the lending rates that are common across all categories of borrowers.
3. Banks may choose any benchmark to arrive at the Base Rate for a specific tenor that may be disclosed transparently.
4. Banks are free to use any other methodology, as considered appropriate, provided it is consistent and is made available for supervisory review/scrutiny, as and when required.
5. Banks may determine their actual lending rates on loans and advances with reference to the Base Rate and by including such other customer specific charges as considered appropriate.
6. In order to give banks some time to stabilize the system of Base Rate calculation, banks are permitted to change the benchmark and methodology any time during the initial six month period, i.e. end-December 2010.
7. The actual lending rates charged should be transparent and consistent and be made available for supervisory review/scrutiny, as and when required.
8. There can be only one Base Rate for each bank. Banks have the freedom to choose any benchmark to arrive at a single Base Rate which should be disclosed transparently.
9. Even after introduction of the Base Rate system, banks **would** have the freedom to offer all categories of loans on fixed or floating rates. Where loans are offered on fixed rate basis, notwithstanding the quarterly review of the Base Rate, the rate of interest on fixed rate loans will continue to remain the

same subject to the condition that such fixed rate should not be below the Base Rate.

10.Applicability of Base Rate: With effect from July 1, 2010, **all** categories of loans should be priced only with reference to the Base Rate. However, the following categories of loans could be priced without reference to the Base Rate: (a) DRI advances (b) loans to banks' own employees (c) loans to banks' depositors against their own deposits. in those cases where subvention is available to borrowers, it is clarified as under :

11.Interest Rate Subvention on Crop Loans: In case of crop loans up to Rupees three lakh, for which subvention is available, banks should charge farmers the interest rates as stipulated by the Government. If the yield to the bank (after including subvention) is lower than the Base Rate, such lending will not be construed to be violative of the Base Rate guidelines. As regards the rebate provided for prompt repayment, since it does not change the yield to the banks on such loans, it would not be a factor in reckoning compliance with the Base Rate guidelines.

12.Interest Rate Subvention on Export Credit: Interest rates applicable for all tenors of rupee export credit advances will be at or above the Base Rate. In cases where subvention is available banks will have to reduce the interest rate chargeable to exporters as per Base Rate system by the amount of subvention available. If, as a consequence, the interest rate charged to exporters goes below the Base Rate, such lending will not be construed to be violative of the Base Rate guidelines.

13.The interest at the specified rates should be charged at monthly rests and rounded off to the nearest rupee.

14. Restructured Loans: In case of Restructured loans if some of the WCTL, FITL, etc. need to be granted below the Base Rate for the purposes of viability and there are recompense etc. clauses, such lending will not be construed to be violative of the Base Rate guidelines.

15.The Base Rate could also serve as the reference benchmark rate for floating rate loan products, apart from external market benchmark rates. The floating interest rate based on external benchmarks should, however, be equal to or above the Base Rate at the time of sanction or renewal.

16.Changes in the Base Rate shall be applicable in respect of all existing loans linked to the Base Rate, in a transparent and non-discriminatory manner.

17.Since the Base Rate will be the minimum rate for all loans, banks are not permitted to resort to any lending below the Base Rate. Accordingly, the current stipulation of BPLR as the ceiling rate for loans up to

Rs. 2 lakh stands withdrawn. It is expected that the above deregulation of lending rate will increase the credit flow to small borrowers at reasonable rate and direct bank finance will provide effective competition to other forms of high cost credit.

18. Banks are required to review the Base Rate at least once in a quarter with the approval of the Board or the Asset Liability Management Committees (ALCOs) as per the bank's practice. Since transparency in the pricing of lending products has been a key objective, banks are required to exhibit the information on their Base Rate at all branches and also on their websites. Changes in the Base Rate should also be conveyed to the general public from time to time through appropriate channels. Banks are required to provide information on the actual minimum and maximum lending rates to the Reserve Bank on a quarterly basis, as hitherto.

19.The Base Rate system would be applicable for all new loans and for those old loans that come up for renewal. Existing loans based on the BPLR system may run till their maturity. In case existing borrowers want to switch to the new system, before expiry of the existing contracts, an option may be given to them, on mutually agreed terms. Banks, however, should not charge any fee for such switch-over.

Interest rates under the BPLR system are applicable to all existing loans sanctioned up to June 30, 2010. However, wherever loans sanctioned up to June 30, 2010 come up for renewal from July 1, 2010, the Base Rate system would be applicable.

Floating Rate of Interest on Loans: Banks have the freedom to offer all categories of loans on fixed or floating rates, subject to conformity to their Asset-Liability Management (ALM) guidelines. The methodology of computing the floating rates should be objective, transparent and mutually acceptable to counter parties. The Base Rate could also serve as the reference benchmark rate for floating rate loan products, apart from external market benchmark. rates. The floating interest rate based on external benchmarks should, however, be equal to or above the Base Rate at the time of sanction or renewal. This methodology should be adopted for all new loans. In the case of existing loans of longer / fixed tenure, banks should reset the floating rates according to the above method at the time of review or renewal of loan accounts, after obtaining the consent of the concerned borrower/s.

Levying of penal rates of interest

Banks are permitted to formulate a transparent policy for charging penal interest with the approval of their Board of Directors. However, in the case of loans to borrowers under priority sector, no penal interest should be charged for loans up to Rs.25,000. Penal interest can be levied for reasons such as default in repayment, non-submission of financial statements, etc. However, the policy on penal interest should be governed by well-accepted principles of transparency, fairness, incentive to service the debt and due regard to genuine difficulties of customers.

Charging of interest at monthly rests: Banks were required to switch-over to the system of charging interest at monthly rests with effect from April 1, 2002. While switching over to the new system, banks were required to ensure that the effective rate does not go up merely on account of the switch-over to the system of charging / compounding interest at monthly rests and increase the burden on the borrowers. Instructions on charging interest at monthly rests shall not be applicable to agricultural advances and banks shall continue to follow the existing practice of charging / compounding of interest on agricultui¯al advances linked to crop seasons. Banks should charge interest on agricultural advances for long duration crops at annual rests. As regards other agricultural advances in respect of short duration crop and allied agricultural activities such as dairy, fishery, piggery, poultry, bee-keeping, etc., banks should take into consideration due dates fixed on the basis of fluidity with borrowers and harvesting / marketing season while charging interest and compounding the same if the loan / instalment becomes overdue. Further, banks should ensure that the total interest debited to an account should not exceed the principal amount in respect of short term advances granted to small and marginal farmers.

Statutory and Other Restrictions

Advance against shares

1. As per Section 19(2) of the Banking Regulation Act, 1949, a banking company can not hold shares in any company, whether as pledgee, mortgagee or absolute owner more than 30% of the paid-up share capital of that company or 30% of paid-up share capital and reserves of the bank whichever is less. RBI has reduced these percentages to 10%.
2. As per Section 20(1) of Banking Regulation Act, banks can not allow advance against their own shares. Further, as per RBI guidelines, banks can not grant advance to their employees for purchase of the bank's own shares.
3. Advance against shares: Maximum advance from the banking system that can be allowed to an individual against shares, convertible bonds, convertible debentures and units of equity oriented mutual funds is restricted to Rs 10 lakh in case of physical shares and to Rs 20 lakh in case of demat shares.
4. Banks should maintain a minimum margin of 50% for finance against both physical and demat shares.
5. Banks can not grant loan against partly paid shares.
6. Banks will not grant loan to partnership/proprietorship concerns against the primary security of shares and debentures.
7. Banks may grant advances to individuals for subscribing to IPOs maximum up to Rs 10 lakh

8. Banks can grant loans to employees of companies for purchasing shares of their own companies under Employees Stock Option Plan(ESOP). Maximum amount of advance can be up to Rs 20 lakh and minimum margin will be 10%.
9. RBI has not prescribed any limit on loan that can be granted to Stock Brokers & Market Makers against shares. It will be as per policy decided by Board of Directors of the respective bank.
10. Banks should maintain minimum margin of 50% while issuing guarantees in favour of stock exchange or commodity exchange on behalf of brokers. Within 50% margin, cash margin should be minimum 25% and balance 25% may be in the form of other securities.
11. Bank's investment in equity shares, Preference shares eligible for capital status, Subordinated debt instruments, Hybrid debt capital instruments issued by other banks should not exceed 10% of the investing bank's capital funds (Tier **I** plus Tier II).
12. Investments made by a bank, in the equity shares, Preference shares eligible for capital status, Subordinated debt instruments, Hybrid debt capital instruments issued by other banks, will attract 100% risk weight for credit risk for capital adequacy purposes.

Loans to Directors of Banks

1. As per Section 20 (1) of Banking Regulation Act, banks can not grant any loans or advances to any of its directors except as permitted by RBI. This rule has. been made applicable to spouse and dependent children of directors also unless spouse has independent source of income.
2. RBI has permitted banks to allow following types of loans to its directors (a) Loan against Government Securities, Life Insurance policies and bank deposit (b) Loans to.employee directors of the bank as are applicable to him as an employee of that bank (c) Facilities like bills purchased/discounted and purchase of cheques (d) credit card facility as per the same criteria as applied to other persons for card business.
3. As per Section 20A of the Banking Regulation Act, 1949, bank can not remit a loan due to the bank by any of its directors without RBI permission.
4. Bank can grant loan to directors of other banks or relatives of its own director or directors of other banks subject to the following conditions:
(a) if loan is less than Rs 25 lac, it can be granted by competent authority but it will be reported to Board of Directors of the sanctioning bank.
(b) If loan is of Rs 25 lac and above it can be granted only with the prior approval of Board of Directors.
5. No officer shall sanction any loan to his relative and should be sanctioned by next higher authority. Credit facilities sanctioned to senior officers of the bank i.e. officers of scale **IV** and above should be reported to the Board_ Credit facility for this purpose does not include advance against Government securities, LIP, fixed or other deposits, temporary overdrafts. upto Rs. 25,000 and purchase of cheques up to Rs. 5,000.

Miscellaneous Instructions

1. Selective Credit Control: RBI can issue directives for restrictions on bank advances against specified sensitive commodities as per provisions of Section 21 & 35A of Banking Regulation Act. Presently Buffer stock of sugar with sugar mills, unreleased stocks of sugar with sugar mills is still covered under stipulations of Selective Credit Control. Banks are free to sanction limits for commodities under the purview of SCC. Banks have freedom to fix interest rate for commodities coming under the purview of SCC.
2. Banks cannot grant loans against CDs or buy-back their own CDs before maturity except in respect of CDs held by mutual funds.
3. Banks should desist from sanctioning advances against FDRs, of other banks.
4. Banks should not grant any advance against bullion/ Primary gold.
5. Banks should not grant loans for acquisition of Small Savings Instruments including Kisan Vikas Patras.
6. Banks can grant loans to the holders of 7% Savings Bonds 2002, 6.5% Savings Bonds 2003 (Non taxable) & 8% Savings (Taxable) Bonds 2003 against pledge or hypothecation or lien of these securities but this facility is not available in respect of the loans extended to third parties.
7. Once a case is filed before a Court I DRT / BIFR, bank should ensure that any settlement arrived at with the borrower is subject to obtaining a consent decree from the Court / DRT / BIFR concerned.
8. Banks may negotiate bills drawn under LCs, on 'with recourse 'or 'without recourse 'basis
9. Banks can not purchase/discount the bills drawn otherwise than under LC on 'without recourse 'basis
10. Banks should not rediscount bills earlier discounted by non-bank financial companies (NBFCs) except in respect of bills arising from sale of light commercial vehicles and two / three wheelers.

Working Capital Requirements and Permissible Bank Finance

Banks are free to adopt their own method of credit assessment. However, for SSI Turnover method will be adopted for limits up to Rs 5 crore.

Turnover Method:

1. This method was suggested by Nayak Committee.
2. This method is to be applied in the case of working capital limits up to Rs 5 crone in the case of

Small Manufacturing enterprises and up to Rs 2 crore in other cases.
3. This method is simple in nature. According to this method, working capital requirement is equal to 25% of the accepted projected annual sales; bank finance is 20% of the projected annual sales or 80% of the working capital requirements and margin is 5% of the projected annual sales or 20% of the working capital requirements. For example, if the current sales are Rs 400 lac, projected growth is 25%, then projected annual sale will be Rs 500 lac. Accordingly, working capital requirement will be Rs 125 lac, bank

finance Rs 100 lac and borrower's margin Rs 25 lac. However, actual drawing power will be allowed as per security available.

4. If net working capital available with the borrower (i.e. borrower's margin) is more than 5% of the projected annual sale, the limits can be adjusted accordingly.

5. The requirement as per this method is minimum assuming working capital cycle of the unit at 3 months. If working capital cycle is more, Bank may consider higher requirement depending on the business of the borrower.

Loan Delivery System

1. This method was suggested by Jilani Committee.

2. This system was made applicable to units with working capital requirements of Rs 10 crore and above from the banking system.

3. Accordingly to this method, 80% of the working capital requirements were to be sanctioned by way of a-demand loan and balance 20% as fluctuating cash credit limit.

4. Later on, **RBI** allowed banks to fix the percentage of demand loan as per their discretion.

5. The method is not applicable in respect of (a) Bill Finance (b) Export credit (c) Seasonal industries (d) sick units —

INCOME RECOGNITION & ASSET CLASSIFICATION

Prudential norms prescribed by RBI include norms relating to Accounting, Exposure, and Capital Adequacy. Prudential accounting norms were implemented in banks in India on the recommendations of Narasimham Committee on financial sector reforms. These relate to income recognition, asset classification and provisioning.

Assets can be categorized into four categories namely (i) Standard (ii) Sub Standard (iii) Doubtful (iv)Loss The last three categories are classified as NPAs based on the period for which the asset has remained non-performing and the realisability of the dues.

(1) **Standard Assets:** The loan accounts which are regular and do not carry more than normal risk. Within Standard assets, there could be accounts which though have not become NPA but are irregular. Such accounts are called as Special Mention accounts.

(ii) Sub-standard Assets: With effect from 31.3.2005, a sub-standard asset is one, which is classified as NPA for a period not exceeding 12 Months (earlier it was 18 months). In such cases, the current net worth of the borrower/ guarantor or the current market value of the security charged is not enough to ensure recovery of the dues to the banks in full. In other words, such an asset will have well defined credit weaknesses that jeopardise the liquidation of the debt and are characterised by the distinct possibility that the banks will sustain some loss, **If** deficiencies are not corrected.

(iii) Doubtful Assets: With effect from 31 March 2005, an asset is to be classified as doubtful, if it has remained NPA or sub standard for a period exceeding 12 months (earlier it was 18 months). A loan classified as doubtful has all the weaknesses inherent in assets that were classified as sub-standard, with the added characteristic that the weaknesses make collection or liquidation in full, - on the basis of currently known facts, conditions and values - highly questionable and improbable.

Doubtful accounts are further classified in three categories namely Doubtful 1 (D1), Doubtful 2 (D2) and Doubtful 3 (D3).

Doubtful 1 or Dl: It is that account which is doubtful up to one year.

Doubtful 2 or D2: It is that account which is doubtful for more than one year but up to 3 year.

Doubtful 3 or D3: It is that account which is doubtful for more than 3 year.

Thus an account remains D1 for 12 months and D2 for 24 months.Loss Assets: A loss asset is one where loss has been identified by the bank or internal or external auditors or the RBI inspection but the amount has not been written off wholly. in other words, such an asset is considered uncollectible and of such little value that its continuance as a bankable asset is not warranted although there may be some salvage or recovery value.

<u>When an account is classified as Doubtful or Loss without waiting for 12 months:</u> If the realizable value of tangible security in an account which was secured in the beginning falls below 10% of the outstanding, it should be classified loss asset without waiting for 12 months and if the realizable value of security is 10% or above but below 50% of the outstanding, it should be classified as doubtful irrespective of the period for

which it has remained NPA.

What is to be done when account becomes NPA?

1. If one account of the borrower in the bank becomes NPA in one branch, then all accounts of that

borrower in other branches of the same bank also are classified as NPA. Thus classification as NPA is done borrowerwise and not accountwise. Only exception to this rule is loan granted to Primary Agricultural Credit Societies.

2. In NPA account, interest or any other charge can be debited to the account only when it is recovered.
3. In all NPA accounts, provision is to be made on the basis of asset classification.

Income recognition — Policy

1. The banks should not charge and take to income account interest on any NPA till it is actually realised.
2. On an account turning NPA, the interest already charged by bank should be reversed or provided for banks to the extent not recovered by debiting Profit and Loss account,and stop further application of interest. However, interest on advances against term deposits, NSCs, IVPs, KVPs and Life policies may be taken to income account on the due date, provided adequate margin is available in the accounts.
3. If Government guaranteed advances become NPA, the interest on such advances should not be taken to income account unless the interest has been realised.
4. If any advance, including bills purchased and discounted, becomes NPA as at the close of any year, the entire interest accrued and credited to income account in the past periods, should be reversed or provided for if the same is not realised. **This will apply to Government guaranteed accounts also.**

CLASSIFICATION AS NPA

Term Loan	If Interest and/ or instalment of principal remain overdue for aperiod of more than 90 days
CC/ Credit/overdraft	the account remains 'out of order or the limit is not renewed/reviewed within180 days from the due date of renewal. Out of order means an account where (i) the balance is continuously more than the sanctioned limit or drawing power OR (ii) where as on the date of Balance Sheet, there is no credit in the account continuously for 90 days or credit is less than interest debited OR (iii) where stock statement not received for 3 months or more. if the bill remains overdue for a period of more than 90 days from due date .
Bills	
Agricultural accounts	(I) if loan has been granted for short duration crop: interest and/or instalment of principal remains overdue for two crop seasons beyond the due date. (ii) if loan has been granted for long duration crop: interest and/or instalment of principal remains overdue for one crop season beyond due date. 1. Decision about crop duration to be taken by SLBC.
Loan against FD, NSC, KVP, LIP	Advances against term deposits, NSCs eligible for surrender, IVPs, KVPs and life policies not treated as NPAs provided sufficient margin is available. Advances against gold
	ornaments, govt securities and all other securities are not covered by this exemption
Loan guaranteed by Government	Loan guaranteed by Central Govt not treated as NPA for asset classification and provisioning till the Government repudiates its guarantee when invoked. Treated as NPA for income recognition. Advances guaranteed by the State Government classified as NPA as in other cases
Consortium advances	Asset classification of accounts under consortium should be based on the record of recovery of the individual member banks.

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· **DISTRESSED ASSETS:**

- Identify incipient stress by creating a sub-category viz., Special mention accounts (SMA) before a loan Account turns into an NPA.
- Early formation of lender's committee with timeline to agree a plan of resolution.
- Incentives for lenders to agree collectively and quickly to plan.
- Improvement in current restructuring process.
- More expensive future borrowing for borrowers who do not co-operate with lenders.
- More liberal regulatory treatment of asset sales.

SPECIAL MENTION ACCOUNTS:

SMA SUB CATEGORY	BASIS FOR CLASSIFICATION
SMA 0	Principal or interest payment not overdue for more than 30 days but account showing signs of incipient stress.
SMA 1	Principal or interest payment overdue between 31 – 60 days.
SMA 2	Principal or interest payment overdue between 61 – 90 days.

SMA-0: IDENTIFIED AREAS

- Delay of 90 days or more in
- Submission of stock statement/ other statements such as QOS, HOS and ABS.
- Credit monitoring or financial statements or
- Non renewal of facilities based on audited financials.
- Actual sales/operating profits falling short of projections accepted by 40% or more.
- A single event of non co-operation /prevention from conduct of stock audits.
- Reduction of Drawing Power (DP) by 20% or more after a stock audit.
- Evidence of diversion of funds for unapproved purpose.
- Drop in internal risk rating by 2 or more notches in a single review.
- Return of 3 or more cheques (or electronic debit instructions) issued by borrowers in 30 days, on grounds of non availability of balance / DP.
- Return of 3 or more bills/cheques discounted or sent under collection.
- Devolvement of Deferred Payment Guarantee (DPG) installments or LCs or invocation of BGs and its non payment within 30 days.
- Third request for extension of time either for creation or perfection of securities or for compliance with any other terms and conditions of sanction.
- Increase in frequency of overdrafts in current accounts.
- The borrower reporting stress in the business and financials.

Promoter(s) pledging/ selling their shares in the borrower Company due to financial stress.

ASSET CLASSIFICATION

1. Asset Classification to be borrower-wise and not facility-wise
2. Assets classified into Standard, Sub standard, Doubtful, Loss. Except standard all others are NPAs.
3. When an account becomes NPA it is called Sub standard asset.
4. An account remains sub standard up to 12 months from the date of becoming NPA

5. Doubtful Assets : An asset is to be classified as doubtful, if it has remained NPA or sub standard for a period exceeding 12 months.

6. Loss Assets : A loss asset is one where loss has been identified by the bank or internal or external auditors or the RBI inspection but the amount has not been written off wholly.

7. When an account is classified as Doubtful or Loss without waiting for 12 months: If in an account which was secured in the beginning, the realizable value of tangible security falls below 10% of the outstanding, it should be.classified loss asset without waiting for 12 months

8. If the realizable value of security is 10% or above but below 50% of the outstanding, it should be classified as doubtful irrespective of the period for which it has remained, NPA.

PROVISIONING NORMS

1. Provisioning is made on all types of assets i.e. Standard, Sub standard, Doubtful and loss assets.

2, Standard Assets :

a. Direct advance to agriculture or Micro and Small Enterprise (Not medium): 0.25% of outstanding; Commercial Real Estate: 1% of outstanding and CRE – Housing – 0.75%

b. Housing Loans with teaser interest rates: 2% of outstanding; All others: 0.4% of outstandinj.

c. The provisions on Standard Assets is shown as 'Contingent Provisions against Standard Assets' under 'Other Liabilities and Provisions Others' in Schedule 5 of the balance sheet.

3. Sub Standard Assets:

a. Secured sub standard: 15% of outstanding balance without considering securities available.

b. Unsecured sub standard: if the loan was unsecured from the beginning: 25% of outstanding balance.

c. If unsecured sub standard for infrastructure: 20% of outstanding balance.

d. Unsecured exposure means exposure where the realisable value of the security, as assessed by the bank/approved valuers/Reserve Bank's inspecting officers, is not more than 10 percent, ab-initio, of the outstanding exposure.

4**. Doubtful Assets:**

1. Unsecured portion:100 %
2. Secured ortion: 20% to 100% depending on the period for which account is doubtful

Age of Doubtful Asset	Provision as % of secured portion
Doubtful up to 1 year D1	25% of RVS (Realisable value of security)
Doubtful for more than 1 year to 3 years; D2	40% of RVS
Doubtful for more than 3 years; D3	100% of RVS

5. **Loss Assets**: 100% of the outstanding amount.
6. If loan is guaranteed by ECGC, CGFT or CGFLHS, provision not on guaranteed portion
7. Provision on advance against FD, NSC, LIP, KVP as per their asset classification.
8. Overall provisions: Provisioning coverage ratio, including floating provisions, should not be less than 70 per cent. Banks should achieve this norm not later than end-September 2010.
9. Provisioning coverage ratio is the ratio of provisioning to gross NPAs.
10. Provision on Standard account to be kept as part of Other Liabilities in Schedule-5 of bank's balance sheet
11. Provision on Standard accounts to be done on Global balance and for NPA accounts on Gross Balance
12. For Doubtful accounts, provision to be done separately for secured portion and unsecured portion of total balance in the account.
13. In case of standard and sub standard assets, provision is on outstanding balance without bifurcating the balance into secured or unsecured.
14. Floating provisions can be deducted from Gross NPAs or treated as part of Tier II capital but not both

SUMMARY OF PROVISIONS PERCENTAGE

Standard - General accounts – 0.40 % Direct Agriculture & SME – 0.25 % Commercial Real Estate – 1.00% easer Home Loans (provision will be 0.4% after one year of increase in interest rate) 2.00% New restructured a/c w.e.f 01.06.2013 : 5% Existing a/c Restructured upto 31.03.2013 wef 31.03.14 (spread over four quarters) : 3.5% wef 31.03.15 (spread over four quarters) : 4.25% wef 31.03.16 (spread over four quarters) : 5.0%	
Sub-standard Secured Sub-standard Unsecured Sub-standard unsecured (infrastructure accounts)	15% 25% 20%

Doubtful - up to 12 months Doubtful - more than 12 months but up to 3 years Doubtful - more than 3 years (secured/unsecured):	25% 40% 100%
Loss account	100%
Provisioning coverage ratio is to be calculated w.r.t. gross NPAs as on Sept 2010 (ratio of provisions / gross NPAs). Excess amount (over and above account-wise provision) to be kept in Cyclical Provision Buffer Account -70%	70%

Important issues relating to provisions : Provision on Standard account to be kept as part of other Liabilities in Schedule-5 of bank's balance sheet (it will be part of tier 2 capital fund for CAR purpose) Provision on Standard accounts to be done on Global Balance and for NPA accounts on Gross Balance For Doubtful accounts provision to be done Separately for secured portion and unsecured portion of total balance in the account.For sub-standard accounts, provision to be done by treating the account secured sub-standard or unsecured sub-standard without bifurcating the balance into secured or unsecured.

Sub-standard unsecured account means an account where at the time of sanction no security obtained or

security value was 10% or less

UPGRADATION OF LOAN ACCOUNTS CLASSIFIED AS NPAs

1. if arrears of interest and principal are paid by the borrower in the case of loan accounts classified as NPAs, the account may be classified as 'standard' accounts immediately.
2. Restructured accounts: After one year after the date when first payment of interest or of principal, whichever is earlier, falls due, subject to satisfactory performance during **12** months period from the date of starting payment after moratorium period. For example, an account was restructured on 5th Jan 2014, moratorium period 6 months, **1st** instalment due on 5th July 2014 which was paid on 1S4 July 2014 and thereafter account was regular for 12 months. This account will be upgraded on 5th July 2015 and not on 1st July 2015.

Gross NPAs: It is the principal dues of NPAs plus Funded Interest Term Loan where the corresponding contra credit is parked in sundry account (Interest Capitalization – Restructured Accounts), in respect of NPAs

NET NPAs: Net NPAs is the amount of Gross NPAs minus

Provisions held in the case of NPA Accounts as per asset classification (including additional provisions for NPAs at higher than prescribed rates)

DICGC/ ECGC claims received and held pending adjustment

Part payment received and kept in Suspense A/c or any other similar accounts

Balance in Sundry Accounts (Interest Capitalization – Restructured Accounts), in respect of NPAs

Floating provisions : Provisions in lieu of diminution in the fair value of restructured accounts classified as NPAs

Provisions in lieu of diminution in the fair value of restructured accounts classified as standard assets

Sale and Purchase of NPAs by banks

1. **The sale and** purchase of NPAs can be made by banks, financial institutions and NBFCs
2. A bank can sell NPA provided it is held in its books as NPA for at least 2 years
3. The sale will be on cash basis and without recourse basis. Purchasing bank can not resell the same to the selling bank.
4. The asset will be classified as Standard Asset in the books of the purchasing bank for 90 days and thereafter on the basis of its record of recovery.
5. Purchasing bank can resell the same other than to the original bank after keeping the same in its books for 15 months
6. The purchasing bank should realize the assets within 3 years. Minimum 10% should be recovered in the first year and 5% in the each following half year.
7. In the books of the purchasing bank, this asset will carry a risk weight of 100% for capital adequacy purpose

Asset Reconstruction Companies

1. **ARCs have been set** up for taking over NPAs from banks\FIs and reconstruct or re pack these for sale
2. First ARC is Asset Reconstruction Company of India Ltd (ARCIL)
3. ARC will be set up as a joint stock company. Registration with RBI is must before commencement of business as ARC.
4. ARC should start business within 6 months of registration with RBI. RElI can extend it by another six months.
5. Net owned funds of ARC should be **15%** of the acquired assets or Rs 100 crore whichever is less.
6. Capital Adequacy Ratio at all times should be at least 15%
7. ARC should invest at least 5% in security receipts created out of each securitization.

Other features

1. Asset Classification to be borrower-wise and not facility-wise. However, in respect of agricultural advances as well as advances for other purposes granted by banks to PACS/ FSS under the on-lending system, only that particular credit facility granted to PACS/ FSS will be classified as NPA and not all the credit facilities sanctioned to a PACS/ FSS.

2. Asset classification of accounts under consortium should be based on the **record of recovery of the individual member banks.**

3. Advances against term deposits, NSCs eligible for surrender, IVPs, KVPs and life policies need not be treated as NPAs provided sufficient margin is available. Advances against gold ornaments, government securities and all other securities are not covered by this exemption.

4. Government guaranteed advances: The credit facilities backed by guarantee of the Central Government will be treated as **NPA** for income recognition. However, asset classification and provisioning would be made only when the Government repudiates its guarantee when invoked. As regards, advances guaranteed by the State Government, with effect from 31^{5t} March 2006, asset classification and provisioning norms and income recognition norms will be applicable as in other cases.

Fair Practices Code for Lenders

All banks/ all India Financial Institutions are advised to adopt the following broad guidelines and frame the Fair Practices Code duly approved by their Board of Directors.The guidelines pertain to:

(i) Applications for loans and their processing
(ii) Loan appraisal and terms/conditions
(iii) Disbursement of loans including changes in terms and conditions
(iv) Post disbursement supervision
(v) General guidelines relating to discrimination on grounds of sex, caste and religion in the matter of lending and harassment in recovery, transfer/takeover of accounts.

ANALYSIS OF FINANCIAL STATEMENTS

Introduction: Before sanctioning a loan proposal a banker collects various details to assess the following:

1. **Net** worth of the applicant i.e. excess of assets over liabilities
2. Repayment capacity based on income, expenditure, repayment of existing borrowings
3. Viability: to ascertain whether bank loan will result in increased earnings for a borrower.
4. Availability of unencumbered securities:

What are financial statements: Basically there are two financial statements namely Balance Sheet and Profit and Loss account. Besides these, Auditor's report, explanatory notes, schedules, and notes on accounts are also obtained wherever available.

A funds flow statement is also prepared to analyse changes in structure of two consecutive balance sheets. Accounting Standard 3 ,makes it mandatory for certain enterprises to prepare cash flow statement. These organizations are which are listed on stock exchange and any other organization with sale turnover of more than Rs 50 crore during the accounting period. These enterprises are also required to do segment wise reporting as per AS --17.

1. A Balance Sheet /Financial Statement is organized collection of information or data prepared as per certain acceptable accounting norms & procedures. Financial statement mainly consists of Balance sheet

(the position of assets and liabilities as on particular date), Profit and loss account (the income and expenditure statement for a Particular period), Funds flow statement & cash Flow statement.

2. Balance Sheet /Financial Statements : 3 stage process - Classification of assets and liabilities (as per RBI guidelines),Calculation of financial ratios Interpretation of ratios.

3. Audited Balance sheet : For credit limit (FB + NFB) upto Rs. 20 lacs no ABS, only unaudited BS but over Rs.20 lacs ABS is must but for Agril. Related loans no ABS upto Rs. 100 lacs & only above Rs. 100 lacs ABS in Agril. Credit (FB + NFB) is required. For company & other statutory body ABS always required irrespective of Quantum of limit and similar in the case in business enterprises where turn over is Rs. 100 lacs or more- ABS. Gross receipt of Profession exceeds Rs.25 lacs- ABS required. As per IT rules Form 3CB & Form 3CD also required where ever it is applicable. In case of sticky accounts S-3, a special audit report is required. Penal Interest of 2% on the outstanding liability shall be collected if ABS is not submitted before 31st oct. every year (within 07 month from closing year) or within a fortnight from the date of Audit of financial accounts of business unit which ever is earlier.

Users of Financial Statements: Banks, Creditors and lenders, investors, Govt agencies, rating agencies, customers, employees, general public, analysts.

Basic concepts used in preparation of financial statements

- Entity concept
- Money measurement concept
- Stable monetary unit concept:
- Going concern concept
- Cost concept
- Conservatism concept
- Dual aspect concept
- Accounting period concept
- Accrual concept
- Realisation concept
- Matching concept

Legal position regarding financial statements

1.Format: (i) For Banking Companies formats are prescribed by Banking Regulation Act. For other companies format of Balance Sheet has been prescribed by Companies Act as per schedule **VI** while no format has been prescribed for profit and loss account. However, as per Schedule **IV** of companies Act, profit and loss account must show specific information. The format of balance sheet may be vertical or horizontal.

A. *Horizontal Form*

Liabilities	Assets
• Share capital	• Fixed assets
• Reserves and surplus	• **Investments**
• Secured loans	• Current assets, loans and advances
• Unsecured loans	• Current assets
• Current liabilities and provisions	• Loans and advances
• Current liabilities	• Miscellaneous expenditures
• Provisions	

B. Vertical Form

I Sources of Funds

1. Shareholders' funds

(a) Share capital
(b) Reserves and surplus

2. Loan funds

(a) Secured loans
(b) Unsecured loans **11**

Application of funds

1. Fixed assets
2. **Investments**
3. Current assets, loans and advances

Less: Current liabilities and provisions Net current assets

4. Miscellaneous expenditures .

2. Accounting period: As per Income tax Act, April to March is the financial year for tax purpose. As per Companies Act it can be different. However, maximum period of the accounting period can be 15 months which can be extended by ROC up to 18 months.

3 For incomplete activity: Every company has to prepare financial statement even if there is no activity during the accounting period or project is not completed.

Balance Sheet

Liabilities defined very broadly represent what the business entity owes others. The Companies Act classifies them as follows:

1. Share capital
2. Reserve and surplus
3. Secured loans
4. Unsecured loans
5. Current liabilities and provisions.

Share Capital: This is divided into two types: equity capital and preference capital. The first represents the contribution of equity shareholders who are theoretically the owners to the firm. Equity capital, being risk capital, carries no fixed rate of dividend. Preference capital represents the contribution of preference shareholders and the dividend rate payable on may be fixed and cumulative. Reserves and surplus : Reserves and surplus are profits which have been retained in the firm. There are two types of reserves: revenue reserves and capital reserves. Revenue reserves represent accumulated retained earnings from the profits of normal business operations. These are held in various forms: general reserve, investment allowance reserve, capital redemption reserve, dividend equalisation reserve, etc. Capital reserves arise out of gains which are; not related to normal business operations. Examples of such gains are the premium on issue of shares or gain on revaluation of assets. Surplus is the balance in the profit and loss account which has not been appropriated to any particular reserve account. Note that reserves and surplus along with equity with equity capital represent owners' equity.

Secured Loans: These denote borrowings of the firm against which specific securities have been provided. The important components of secured loans are: debentures, loans from financial institutions, and loans from commercial banks.

Unsecured Loans: These are the borrowings of the firm against which no specific security has been provided. The major components of unsecured loans are: fixed deposits, loans and advances from promoters, inter-corporate borrowings, and unsecured loans from banks.

Current Liabilities and Provisions: Current liabilities and provisions, as per the classification under the Companies Act, consist of the following: amounts due to the suppliers of goods and services bought on credit; advance payments received; accrued expenses; unclaimed dividend; provisions for taxes, dividends, gratuity, pensions, etc. Current liabilities for managerial purposes (as distinct from their definition in the Companies Act) are obligations which are expected to mature in the next twelve months. So defined, they include the following:

(i) loans which are payable within one year from the date of balance sheet,

(ii) accounts payable (creditors) on account of goods and services purchased on credit for which payment has to be made within one year,

(iii) Provision for taxation for taxation,

(iv) accruals for wages, salaries, rentals, interest, and other expenses (these are expenses for services that have been received by the company but for which the payment has not fallen due), and

(v) advance payment received for goods or services to be supplied in the future.

Assets

Broadly speaking, assets represent resources which are of some value to the firm. They have been acquired at a specific monetary cost by the firm for the conduct of its operations. Assets are classified as follows under the Companies Act:

1. Fixed assets
2. Investments
3. Current assets, loans and advances

4. Miscellaneous expenditures and losses

Fixed Assets: These assets have two characteristics: they are acquired for use over relatively long periods for carrying on the operations of the firm and they are ordinarily not meant for resale. Examples of fixed assets are land, buildings, plant, machinery, patents, and copyrights.

Investments: These are financial securities owned by the firm. Some investments represent long-term commitment of funds. (Usually these are the equity shares of other firms held for income and control purposes). Other; investments are short-term in nature and may rightly be classified under current assets for managerial purposes. (Under requirements of the Companies Act, however, short-term holding of financial securities also has to be shown under investments, and not under current assets).

Current assets, loans, and advances: This category consists of cash and other resources which get converted into cash during the operating cycle of the firm. Current assets are held for a short period of time as against fixed assets which are held for relatively longer periods. The major components of current assets are: cash, debtors, inventories, loans and advances, and pre-paid expenses. Cash denotes funds readily disbursable by the firm. The bulk of it is usually in the form of bank balance; the rest comprises of currency held by the firm. Debtors (also called accounts receivable) represent the amounts owned to the firm by its customers who have bought goods, services on credit. Debtors are shown in the balance sheet at the amount owed, less an allowance for the bad debts. Inventories (also called stocks) consist of raw materials, work-in-process, finished goods, and stores and spares. They are usually reported at the lower of the cost or market value.

Loans and advances: are the amounts loaned to employees, advances given to suppliers and contractors, and deposits made with governmental and other agencies. They are shown at the actual amount. Pre-paid expenses are expenditure incurred for services to be rendered in the future. These are shown at the cost of unexpired service.

Miscellaneous expenditures and losses: This category consists of two items: (i) miscellaneous expenditures and (ii) losses. Miscellaneous expenditure's represent certain outlays such as preliminary expenses and pre-operative expenses which have not been written off. From the accounting point of view, a loss represents a decrease in owners equity. Hence, when a loss occurs, the owners' equity should be reduced by that amount. However as per company law requirements, the share capital (representing owners' equity) cannot be reduced when a loss occurs. So the share capital is kept intact on the left hand side (the liabilities side) of the balance sheet and the loss is shown on the right hand side (the assets side) of the balance sheet **Profit And Loss Account**

It is a statement of income and expenditure for a accounting period. The items of P& L account are:

- Gross and Net sales
- Cost of goods sold
- Gross profit
- Operating expenses
- Operating profit
- Non-operating surplus/deficit
- Profit before interest and tax
- Interest
- Profit before tax
- Tax
- Profit after tax (Net Profit)

Gross and Net Sales:Total price of goods sold is called Gross sales. Net sales are Sales minus excise duty. Cost of goods sold is the sum of costs incurred for manufacturing the goods sold during the accounting period. It consists of direct material cost, direct labour cost, direct labour cost, and factory overheads. It should be distinguished form the cost of production. The latter represents the cost of goods produced in the accounting year, not the cost of goods sold during the same period.

Gross profit is the difference between net sales and cost of goods sold. Most companies show this amount as a separate item (as in the table here). Some companies, however, show all expenses at one place without making gross profit a separate item.

Operating expenses consist of general administrative expenses, selling and distribution expenses, and depreciation. (Many accountants include depreciation under cost of goods sold as a manufacturing overhead rather than under operating expenses. This treatment is also quite reasonable).

Operating profit is the difference between gross profit and operating expenses. As a measure of profit it reflects operating performance and is not affected by non-operating gains/losses, financial leverage, and tax factor. Non-

operating surplus represents gains arising from sources other than normal operations of the business. Its major components are income from investments and gains from disposal of assets. Likewise, non-operating deficit represents losses from activities unrelated to the normal operations of the firm.
Profit before interest and taxes is the sum of operating profit and non-operating surpiusideficit. Referred to also as earnings before interest and taxes (EBIT), this represents a measure of profit which is not influenced by financial leverage and the tax factor.
Interest is the expenses incurred for borrowed funds, such as term loans, debentures, public deposits, and

working capital advances.
Profit before tax is obtained by deducting interest from profits before interest and taxes.
Tax represents the income tax payable on the taxable profit of the year.
Profit after tax is the difference between the profit before tax and tax for the year.
Dividends represent the amount earmarked for distribution to shareholders.
Retained earnings are the difference between profit after tax and dividends.

Funds Flow Statement / Cash Flow Statement

All items on the liability side represent source of funds and all items on the asset side except cash represent use of funds. Cash represents unutilized portion of funds available to the firm. If cash represents use of funds then all uses of funds are equal to source of funds. Comparison of two balance sheets of different dates will indicate that in every item there may be a increase or decrease in funds. Increase in any item on liability side or decrease in asset side item, represents increase in funds. Decrease in any item on liability side or increase in any item on asset side represents decrease in funds. A statement of these changes is called Funds flow statement. Normally the intervening period is a financial year. For preparing cash flow statement, start with cash in the first balance sheet as opening balance, add all additional sources excluding cash and deduct all additional uses excluding cash which will be equal to cash shown in the second balance sheet. There is difference between cash budget prepared for assessing the need for working capital funds from the bank.

PURPOSE OF FINANCIAL STATEMENT ANALYSIS

Financial statement analysis can be used by the different users and decision makers to achieve the following objectives:

1. Assessment of Past Performance and Financial Position: An analysis of the financial statements reveals the trend of growth of its business and its profitability. By comparing these to industry trend, opinion about **the management and** efficiency of the enterprise is **formed. Financial statements reveal composition of assets and liabilities. Financial health can be judged by seeing the trend of leverage (Debt/equity), retention of profits etc.**

2. Projection of Future Performance: Past performance is often a good indicator of future performance. Financial analysis helps in projecting the earning prospects and growth rates in the level of activity and earnings with a reasonable degree of certainty.

3. Detecting Danger signals: It helps in detecting any deterioration of its financial health. Bank can accordingly take preventive measures to avoid/minimize losses.
4. Assessment of credit requirements: Financial analysis helps in assessing credit requirements more accurately. It also helps in assessing the repayment schedule, credit risk, decide terms and conditions of loan.
5. Examine funds flow: To know if there is any diversion of funds and any mismatch in liquidity position.
6. Cross Checking: Statement of stocks and book debts given for calculating drawing power are cross checked with figures given in the balance sheet.

REARRANGING FINANCIAL STATEMENTS

Balance Sheet: Liabilities side is regrouped in Net worth, Long Term Liabilities, Current Liabilities and Provisions. Assets are regrouped into Fixed assets, Current assets, Non current assets, Intangible assets. Profit and Loss account is rearranged as per format prescribed under erstwhile Credit Monitoring Arrangement (CMA).

Focus of Financial Statement Analysis

Financial Statement Analysis involves evaluating different aspects of a business enterprise which are of great

importance to different users such as management, investors, creditors, bankers, analysts, investment advisers, etc. Generally, the following analyses are made while making financial statement analysis:

I. Liquidity or Short-Term Solvency Analysis

Profitability Analysis

III. Capital Structure or Gearing Analysis

IV. Market Strength or Investor Analysis

V. Growth and Stability Analysis

Techniques used in Analysis of Financial Statements:

Various techniques are used in the analysis of financial data to emphasise the comparative and relative importance of data presented and to evaluate the position of the firm. Three methods are used:

1. Funds flow analysis

2.Trend Analysis

3. Ratio Analysis

1. Funds flow analysis: Sources and Uses of funds are classified as Long Term and Short Term. If short term sources are more than short term uses it indicates diversion of funds and needs to be enquired. However,

sometimes when current ratio is very high it is desirable. 7,520 4.5%

2. Trend Analysis: Horizontal analysis: The items for which trend is to be seen are arranged in horizontal form and percentage increase or decrease over previous year is indicated. Broadly trend in sales, operating profit, PBT, PAT are analysed from profit and loss account. Similarly Balance sheet items are compared. (ii) Common Size statements: are prepared to express relationship _of various items to one item in percentage term. For example, raw material as percentage of sales for various years indicates operating efficiency.

3. Ratio Analysis: A ratio is comparison of two figures and can be expressed as percentage or number or a proportion. Figures used in ratio can be from profit and loss account or balance sheet or a combination of profit and loss account and balance sheet. Ratios help in. comparing financial position and financial performance with others as its own performance over the years. Main .ratios of interest to banker are given below:

Terms used in Financial statement analysis

1	Net Sales	Gross Sales minus returns, discounts, excise duty.
2	Raw Materials consumed	Opening Stock of raw materials plus purchases of raw materials less Dosing stock of raw material .
3	Cost of Production	Raw materials consumed, stores and spares consumed, power and fuel, direct labour, repairs and maintenance, other manufacturing expenses and depredation plus opening stock of stock in process minus dosing stock of stock in process.
4	Cost of Sales	Cost of production (3) plus opening stock of finished goods minus dosing stock of finished goods.
5	Gross Profit	Net Sales - Cost of Sales (Item 1 minus Item 1)
6	Operating Profit	Gross Profit (5) minus interest, selling general and administrative expenses.
7	Net Profit before tax	Operating profit plus other incomes minus other expenses
8	Net Profit after tax	Profit before taxation minus provision for taxes.
9	Retained Profit	Net profit minus dividend paid / dedared
10	Cash Profit	Profit before charging Depreciation (Net Profit + Depredation)
11	Cash-Loss	Loss before charging Depredation (Net Loss — Depredation)
_12	Assets	Things owned by a business Not converted into cash in normal course

13	Fixed Assets .	of business, These are acquired to use them in the production of other goods and services.
14	Current Assets	Assets which are meant to be converted into cash or consumed in normal course of business say within 1 year. These are also called as gross working capital.
15	Intangible Assets .	Expenditure on invisible assets, likely to yield benefit to the company in future e.g. goodwill, patent, trade marks, designs.
16	Fictitious Assets	Which have notional value only e.g. losses, preliminary expenses.
17	Miscellaneous Assets or Non current assets	Which can't be classified as current, fixed or intangible e.g. inter Corporate investment
18	Tangible Assets	Total asset side of balance sheet minus intangible assets.
19	Quick Assets	Assets which can be converted to cash quickly. Cash, bank balances, marketable investments, bills receivables and sundry debtors considered goal. (Current Assets minus-Inventories & Prepaid Expenses)
20	Liabilities	Things owed by the business.
21	Owners Equity (Net Worth)	Paid up share capital, reserves and surplus, preference shares with more than 12 years maturity.
22	Long term liabilities or Debt	Outsiders funds, payable in more than 12 months. Term loan (exduding instalment payable within 12 months) plus debentures maturing within more than one year, preference shares redeemable within 12years, deposits payable beyond one year.
23	Current Liabilities	Liabilities which are payable in less than one year e.g. sundry creditors, unsecured loans, advances from customers, interest accrued but not due, dividends payable, statutory liabilities, provisions, Bank borrowings for working capital etc
24	Total Outside Liabilities	Total of the liability side of balance sheet minus net worth
25	Tangible Net Worth	Total tangible assets minus total outside liabilities. Owner's funds minus Intangible & Fictitious assets ; Paid up capital plus reserves minus intangible assets
26	Gross Working Capital	Total of Current Assets
27	Net Working Capital	Current assets minus total current liabilities **or** Long Term Sources minus long term uses
28	Working Capital gap	Current Assets minus current liabilities other than Bank Borrowings.
29	Long term sources	Paid up capital, reserves and surplus (excluding specific reserves) i.e. Net Worth and long term liabilities.
30	Short Term Sources	Current Liabilities
31	Long Term Uses	Fixed Assets, Miscellaneous or Non. current assets, Intangible and Fictitious Assets (assets other than current assets)
32	Short Term Uses	Current Assets
33	Contingent Liabilities	Likely liability which may or may not arise on the happening or non happening of an event

(i) As per RBI guidelines, installments of term loans due within 12 months are not to be treated as current liability for calculation of Net Working Capital and Working Capital Gap. (ii) Overdue instalments and Interest on term loan is treated as current liability. (iii) Sundry Debtors/ Book debts older than 6 months are treated as Non current assets. (iv) Loans from friends and relations are normally treated as Long term liability but if these are secured by Demand Promissory Note i.e. payable on demand then the same should be treated as Current Liability. (v)Reserves except which are in the nature of provisions like Depreciation Reserve are part of net worth.

Liabilities	Assets
Net worth/Equity Funds brought in by the promoters as their investment in business or generated by and retained in business Share capital/partner's capital/ Paid up equity share capital,/owners funds Reserves & Surplus e.g. General Reserve, Capital Reserve, Revaluation Reserve and Other Reserves),Retained Earnings Undistributed Profits,Preference share capital (not redeemable within 12 years)	Fixed Assets :Assets which are purchased for long term and not meant to be sold but used for production. Land & Building,Plant & Machinery Vehicles,Furniture & Fixture Office equipment,Capital Work in Progress These are represented as under: Original value (Gross Bock) Less depreciation Net Block or book value or written down Value Method
Long term liabilities: Liabilities which are not due for payment within 12 months from the date of the Balance Sheet) Term loans from financial institutions; Term loan from banks; Debentures/Bonds; Deferred payment liability;Preference Shares redeemable within 12 years; Fixed Deposits maturing after one year; Provision for gratuity; Unsecured Loans	Non Current Assets: Assets which cannot be classified as current or fixed or intangible assets Book Debts or Sundry Debtors more than 6 months old/ Disputed Debts, Investment of long term nature in shares, govt. securities, associates or sister firms or companies. Long term security deposits. Unquoted investments; Investments in subsidiaries or sister concerns; Loans & Advances to directors, officers; Accounts receivables in respect of sale of plant & machinery; Advances to concerns in which directors are interested; Deposits with customs port trust etc Intangible & fictitious Assets Which do not have physical existence. For example: Goodwill, Patents, Trade Mark, Copy Right, Preliminary or pre operative expenses, other formation expenses, debit balance of P & L account, accumulated losses, bad debts, Capital issue expenses e.g. discount on issue of share & debentures, commission on underwriting of shares & debentures; Deferred revenue expenditure e.g. Advertisement
Short term for CurrentyLiabilities Liabilities which are due for payment within 12 months from the date of the balance sheet and are to be repaid out of proceeds of current assets,Short term borrowings from banks (C/C, 0/D or B/P, B/D limits) for working capital.,Sundry/trade creditors/creditors/ Account payable,Bills Payable / trade acceptances Fixed Deposits from public payable within one year,Short duration loans or deposits Provision for taxation, Proposed Dividends, Provision for bonus, unclaimed dividend. Deposits from dealers, selling agents etc. Advance payments from customers, outstanding expenses and Accruals e.g. wages & salaries, rent; expenses payable	Current Assets : Cash in hand, Bank balance including fixed ,deposits with banks. Stocks/inventory (such as raw material, stock in process, finished goods, consumable stores and spares),Book debts/Sundry debtors/Bills Receivable/ Accounts receivable/ debtors, Government and other trustee securities (other than for long term purposes e.g. sinking funds, gratuity funds etc.),Readily Marketable/quoted govt. or other securities meant for sale,Interest accrued and receivables,Advance payment of taxes, pre-paid expenses,Advance payments for merchandise; unexpired insurance

TOTAL	TOTAL

RATIO ANALYSIS

How ratios are expressed : Ratios can be expressed in the following different ways: In %age terms such as net profit to sale ratio (being 23%),In proportion such as current ratio (being 2:1),In no. of times such as stock turnover ratio (being no of times)

Classification of ratios

The ratios can be classified as (a) Traditional ratios (b) Functional ratios:

1. **Traditional classification —** It is based on the source of information from financial statements. It can be

(a) Profit and loss account ratios (where information is taken from P & L account

(b) Balance **sheet ratios** (where the source of information is balance sheet and

(c) Composite ratios or inter-statement ratios (where the information is taken from profit and loss account and the balance sheet.

2. Functional classification : When ratios are classified on the basis of how they serve as a tool for analysis. This can be:

(a) Profitability ratios

(b) Activity ratios or turnover ratios

(c) Solvency or leverage ratios or financial ratios. These can be short term solvency ratios like current ratio or long term solvency ratios like debt equity ratio.

Types of ratios

As a banker, one would normally depend upon four types of ratios namely:

a: Liquidity ratios,
b: Leverage or solvency ratios,
c: Profitability ratios,
d: Activity ratios.

LIQUIDITY RATIOS

The ratio which indicate the liquidity of the firm are current ratio, acid test ratio or quick ratio and net working capital.

1. Current Ratio

The current ratio is the relationship between the current assets and current liabilities. The ratio helps in knowing about the liquidity position of a firm during the course of a year. It can be worked out as under:

Current assets / Current liabilities

2. Acid Test or Quick Ratio or Liquidity ratio

The quick ratio is the ratio between quick current assets and current liabilities. The ratio measures the capacity of the organisation to pay off current liabilities of the urgent nature immediately.

Quick assets include cash/bank balances + receivables upto 6 months + quickly realisable securities such as govt. securities or quickly marketable/quoted shares and bank fixed deposits. It can be worked out as under:

Quick assets I Current liabilities

If the cash and bank balances are Rs.2 lac, receivables Rs.5 lac, quickly realisable securities Rs.1 lac and current liabilities Rs.10 lac, the quick ratio would be 0.8:1.

LEVERAGE OR SOLVENCY RATIOS

The long term solvency can be judged by solvency ratios, most importance of which, is debt-equity ratio and debt service coverage ratio (DSCR).

1. Debt Equity ratio

The ratio is important one since it shows the dependence of the unit on outside long term finance. A debt-equity ratio of 2:1 is considered desirable by the banks and Reserve Bank. It can be worked out as under:

Long term outside liabilities/Tangible net worth

(Where long term outside liabilities are liabilities of long term nature and tangible net worth is total of capital and reserves and surplus reduced by intangible assets.

Interpretation — Higher the ratio, more the pressure on the liquidity of the organisation, when repayment of liabilities falls

due. Lower the debt equity of a firm compared to another firm, the better it is.
For instance, if a firm is having capital of Rs.200 lac, the free reserves and surplus of RS.300 lac and long term loans or liabilities of Rs.800 lac, the debt equity ratio would be 1.6:1. Similarly when the Debt equity ratio for a firm declines say from 1.6 : 1 to 1.2:1, it is considered better.

2. Fixed Assets Ratio : Ratio is calculated as : Fixed Assets / Long term funds.(Fixed assets include net fixed assets and trade investments and long term funds include capital, reserves and long term loans)

3. Debtor service coverage ratio (DSCR)

The ratio explains the relationship between the funds available for servicing the long term outside liabilities (where servicing means regular payment of interest on long term liabilities and also payment of due amount of principal on year to year basis) on the one hand and amount of interest and instalment of long term outside liabilities on the other side. This ratio is used for judging repayment capacity and fixing the repayment schedules for term loans in banks and financial institutions.
It could be worked out by taking into account net profit + depreciation + annual amount of interest charged (or chargeable) on the long term liabilities / annual amount of interest charged (or chargeable) on the long term liabilities + annual amount of instalment payable on the long term liabilities. For instance, if a firm's net profits are R..5.3 lac, depreciation Rs.2 lac, interest payment Rs.1 lac and the annual instalment Rs.2 lac, the DSCR would be 2 ((3+2+1) / (1 + 2)
Generally the banks or financial institutions consider a DSCR at 2 as comfortable.
Tangible net worth = Net worth less intangible assets
Tangible assets = Total assets less intangible assets

ACTIVITY RATIOS

These ratios measure the efficiency of the organisation in using deploying the available funds, particularly the funds raised on short term basis. The following ratios could be worked out:

a: Inventory turnover:

Sales / Average stocks (average of opening and closing stocks) (it can also be calculated as **cost of sales / average stock)**

b: Debtor turnover :

Sales / average debtors (average of opening and closing receivables) (it can also be calculated as credit sales / average debtors).

c: Fixed assets turnover :

Sales / Fixed assets.

d: Current assets/ working capital turnover

Net sales / average working capital i.e. current assets
If the amount of net sales in firm is Rs.200 lac and the average working capital Rs.50 lac, the working capital turnover ratio would be 4 (200/50). In the following year if the ratio comes down to, say 3, it reflects inefficiency in use of working capital by the firm.

e: Debtors' velocity or debt collection period

Average Book-debts / sales x 12 (can be calculated as average Book-debts / credit sales x 12) This ratio indicates as to how much time the firm is taking in recovering the amount of credit sales.

PROFITABILITY RATIOS

Profitability indicates the efficiency of the organisation in generation of income and surplus out of the operations of main business.

1. Return on investment or Return on capital employed or Overall Profitability Ratio)

This is the basic profitability ratio and can let us know, as to how much the organisation is earning on its capital employed. The ratio can be worked out as under:

Profit before tax and interest / Investment (or capital employed) x 100

Where, the 'return' is net profit before interest & tax and `investment or capital employed' means tangible net worth of the share holders' funds and outside term liabilities.

For example, if the net profits before tax are Rs.30 lac and the investment Rs.120 lac, the return on investment shall be

25% (30 / 120 x 100).

2. Return on equity

This ratio provides information about the earnings, which the funds put in by the promoters/shareholders or the ones retained in the business, generate. The ratio can be worked out as under:

Net profits / owned funds (or tangible net worth) x 100

For example if the net profits are Rs.3 lac and tangible net worth Rs.10 lac, the return on equity would be 30%.

3. Gross Profit & Net Profit Ratio

The **gross profit** is considered to be the surplus of sales over the cost of goods sold and the ratio can be worked out as under:

Gross Profit / Net Sales x 100

4. The **net profit** is the surplus of gross profit after meeting other expenses. This can be before tax or after tax and is finally appropriated to meet the tax liability (if taken before tax provisions), dividend payment or drawings and to retain a part in the business, which is converted into the capital employed. The ratio can be worked out as under:

Net profit* / Sales x 100 (*The net profit could be before or after tax.)

5. Operating Profit ratio

The ratio denotes the margin of profit on the main operations revealing the operational efficiency of the unit. The ratio is worked out, to see that the main activity remains viable for long time, as under:

Operating Profit / Sales x 100

where the operating profit represents profit minus net other income or profit from un-related activity.

6. Earning Per Share (EPS) :

The ratio denotes per share profit of a company. It can be used to compare 2 different companies'' profitability. To calculate the ration only the no. of equity share is taken (and not of preference shares). It can be calculated as under: **Net profit after tax and preference dividend/ no. of equity shares.**

It help in understanding market pricing of the equity share.

6. Price Earning Ratio (PER)

The ratio indicates the current market price vis-a-vis the earning per share. It can be calculated as under:

Market price of the equity share / earning per share

Different users of ratios

Long term creditors	Short term lenders (Banks)	Shareholders
Fixed charges cover = ncome beforeinterest andtax / Interest charges	Quick ratio --- Quick assets / current liabilities	Earning per share = Profit available for equity holders / no. of equity shares
Debt service coverage ratio = Cash profit for debt service / annual interest and principal	Current ratio = Current assets / current liabilities	Dividend Yield ratio = Dividend per share / market price per share

WHAT THE CHANGE IN RATIOS MEAN

If a firm realises book debts in cash — No change in current assets, quick ratio, current ratio or net working capital.

If a firm realises old assets **or non current assets in cash or sell fixed assets in cash:** current assets, quick ratio, current ratio or net working capital will all improve

If a firm issues bonus shares — There is no change in any ratios

If a firm issues rights shares — Current ratio, quick ratio, net working capital, debt equity ratio, net worth will improve

If a firm revalues its fixed assets and creates revaluation reserve: Net worth and tangible networth increase. Debt equity ratio declines / improves. There is no effect on current assets or quick assets or current ratio and quick ratio.

If increase in long term sources is more (say 125%) than increase in long term uses during a year liquid asset would increase, liquidity would improve.

If increase in long term is uses more (say 125%) than increase in long term sources during a year — liquid asset would decrease, liquidity would decline.

Lower and higher break even point : A firm with lower break even point has better chances for earning profits. A firm with higher break even earns lower profits.

If break-even point of a firm goes up — It is an indication of dedine in profits

If break-even point of a firm goes down — It is an indication of increase in profits

If debtor-turnover ratio increase — It shows efficiency in recovery

If debtor-velocity ratio decrease — It shows firm is allowing credit to buyer of its products for a lesser period

If stock-turnover ratio increase — It is better use of stocks

If current ratio increases and quick ratio remain constant — It shows higher %age of stocks in or lower %age of receivables in total current assets.

If current ratio is constant and quick ratio increases — It shows lower %age of stocks or higher %age in receivables in total current assets.

PRACTICE TEST

Classify the following assets and liabilities for Balance Sheet of M/s Gopala & Govinda Company for the year as on 31.3.2012.

Cash	200	Good will	300
Provision for Expenses	200	Capital	2000
Vehicles	1000	Sundry Debtors	1600
Unsecured loans (Long term)	800	Term Loan	2000
Investment in other firms	300	Plant and Machinery	2500
Pre Operative Expenses	200	Sundry Creditors	1200
Stocks	2000	Reserves	1000
Prepaid expenses	200	Expenses payable	200
Security Deposit	200	Bank Borrowings / cash credit	1400
Land and building	1500	Debentures	1200
Sales	10000	Net profit	500
Interest on Term Loan	300	Depreciation	200

Calculate Current Ratio / Quick Ratio / Net working Capital / Debt Equity Ratio / Debt Service Coverage (consider that installment during the year is 400) Ratio / Stock turnover ratio / Debtor Turnover ratio / Debtor velocity ratio / Net profit %.

Answer:

LIABILITIES	`	**ASSETS**	
OWNERS FUNDS		**FIXED ASSETS**	
Capital	2000	Land and Building	1500
Reserves	1000	Plant and Machinery	2500
B TOTAL(Net Worth)	**3000**	Vehicles	1000
LONG TERM LIABILITIES		**SUB TOTAL(Fixed Assets)**	**5000**
Unsecured Loans	800	**NON CURRENT ASSETS (NCA)**	
Term Loan	2000	Investment in Firms	300
Debentures	1200	Security Deposit	200
SUB TOTAL(Term Liabilities)	**4000**	**SUB TOTAL (Total Non Current Assets)**	**500**
CURRENT LIABILITIES		**INTANGIBLE ASSETS**	
Provision for Expenses	200	Goodwill	300
Sundry Creditors	1200	Pre Operative Expenses	200
Expenses Payable	200	**SUB TOTAL(Total Intangible Assets)**	**500**

Bank Cash Credit	1400	**CURRENT ASSETS**	
SUB TOTAL(Current Liabilities)	**3000**	Cash	200
		Sundry Debtors	1600
		Stocks	2000
		Prepaid Expenses	200
		Total Current Assets - Subtotal	**4000**
GRAND TOTAL (Total of Liabilities)	**10000**	**GRAND TOTAL (Total of Assets)**	**10000**

Calculations:

Networth	Capital + Reserves	2000+1000	3000
Intagible assets			500
Tangible NW	NW - Intangibles	3000 – 500	2500
Long Term Liabilities			4000
Long Term Sources	LTL + Networth	4000+3000	7000
Current Liabilities			3000
Short Term Sources	(= Current Liabilities)		3000
Outside Liabilities	(= LTL + CL)	4000+3000	7000
Long Term Uses	= Fixed Assets+ NCA+ Intangible Assets	5000+500+500	6000
Current Assets			4000
Gross Working Capital	(= Total CA)		4000
Short Term Uses	(CA)		4000
Net Working Capital	CA – CL	4000-3000	1000
Quick Assets	CA –Stocks& Prepaid Exp	4000-2200	1800
Current Ratio	CA ÷ CL	4000 ÷ 3000	1.33:1
Quick Ratio	QA ÷ CL	1800 ÷3000	0.66:1
Debt Equity Ratio	LTL ÷ TNW	4000 ÷ 2500	1.66:1
DSCR	(Profit + Depreciation + TL Interest) ÷ (TL Installment + TL Interest)		
	500+200+300 = 1000	14	(1000÷700)
	400+300 = 700		
Stock Turnover Ratio	Sales ÷ Stocks	10000 ÷ 2000	5 times
Drs T/o Ratio	Sales ÷ Sy Debtors	10000÷1600	6.3 times

Debtors Velocity Ratio	(Sy Drs÷Sales) x 12	(1600÷10000) X 12	1.92 months
Net Profit %	(NP ÷ Sales) x 100	(500 ÷ 10000) x 100	5%
Return on NW	(NP ÷ TNW) x 100	500 ÷ 2500 x 100	20%

WORKING CAPITAL FINANCE

CONCEPT OF WORKING CAPITAL

Working Capital is defined as the excess of current assets over current liabilities. It is the same as net current assets. It represents the investment of a company's funds in assets which are expected to be realised within a relatively short period of time. It is not an investment in an asset with a long life but, as the name implies, represents funds which are continually in use and are turned over many times in a year. It is capital used to finance production, to support levels of stock and to provide credit for customers. The three main current assets are stock, debtors and cash. They can be funded by short-term finance, i.e. current liabilities, or by medium and long-term finance in case of permanent current assets or core current assets.

Components of Working Capital

The firm's Working Capital may be viewed as being comprised of two components:

1. Permanent working capital: These funds represent the current assets required on a continuing basis over the entire year. it represents the amount of cash, receivables and inventory maintained as a minimum, to carry on operations at any time, as a safety measure.
2. Variable working capital: These funds represent additional assets required at different times during the operating year. Added inventory must be maintained to support the peak selling periods. Receivables increase and must be financed following periods of high sales. Extra cash may be needed to pay for increased supplies preceding high activity.

Working Capital Cycle

Working Capital cycle is the length of time that elapses between the company's outlay on raw materials, Wages and other expenditures and the inflow.of cash from the sale of the goods. The length of the cycle depends upon

(I) stock of raw material required to be held.

(ii) The work in process which depends on the process involved in manufacturing or processing the raw material.

(iii) Credit required to be provided to the purchasers.

Longer the working capital cycle, the more is the working capital requirement i.e. need for maintaining the current assets.

Working capital & Net working Capital Working capital (or gross working capital) refers to the amount of total current assets.

Liquid surplus or net working capital refers to the surplus of long term sources over long term uses as per RBI prescription (also calculated by banks as difference between current assets and current liabilities). It is desirable, that the net working capital should be positive which would signify liquidity and availability of. Adequate working funds. If in a particular case, the net working capital is negative, the difference will be called the working capital deficit.

The working capital can also be classified as:

a Permanent working capital which is minimum amount of current assets necessary for carrying out operations for a period.

b Fluctuating working capital : Additional assets required at different times during an operating period due to cyclic factors.

c Seasonal working capital means requirement for additional current assets due to seasonal nature of the industry.

d Adhoc working capital : Additional funds for meeting the needs arising out of special circumstances e.g. execution of special order, delay in receipt of payment of receivables.

e Working capital term loan : A long term loan given to meet the working capital margin needs of a borrower. The concept was introduced by. Tandon Committee.

f Working capital gap = total current assets less other current liabilities. It is financed by net working capital and bank finance for working capital (called MPBF).

SUMMARY - WORKING CAPITAL TERMS

Particulars	Classification
Working capital	Current assets such as cash, stocks, book-debts, other current assets
Net working capital	Current assets — current liabilities OR Long term sources — long term uses
Working capital gap	Current assets — current liabilities (other than bank borrowing — i.e. OCL)
Working capital limits	ank facilities needed to purchase current assets. These facilities are cash credit, overdraft, bills purchase/discounting, pre-shipment or post-shipment loans etc.

Factors which determine the working capital The following factors determine the overall working capital levels of the industrial units: Policies for production, Manufacturing process, Credit Policy of the unit, Pace of turnover , Seasonality

Process for assessment of working capital requirements Generally there are three methods followed by banks for assessing working capital of a firm i.e. (i) traditional method suggested under Tandon Committee, (ii) turnover method suggested by Nayak Committee and (iii) cash budget method followed in case of seasonal industries.

Methods of Assessing Bank Finance

Holding Norms based Method of Assessment of Bank Finance Various steps used in the process include following

(a) Deciding on the level of turnover: : in case of existing units, past performance can help in ascertaining projected turnover. In case of new enterprise, it is based on production capacity, proposed market share, availability of raw materials, industry norms etc.

(b) Assessment of Gross working capital: This is sum total of various components of working capital

(i) inventory: For assessment of stock levels of raw material, work in process and finished goods, information like lead time, minimum order quantity, location and number of suppliers, percentage of imported material, manufacturing process etc are considered. Industry norms may be helpful in this regard.

(ii) Receivables/bills: it can be assessed easily. It is governed by market practice relating to a particular business.

(iii) Other Current assets: A reasonable estimate of other current assets like cash level, advance to suppliers, advance tax payment etc is calculated. Sources of Meeting Working Capital Requirement

(i) Own sources: This represents available net working capital. Further, as the estimate of limits is based on the projected balance sheet at the end of the current accounting year, some internal accruals are also taken into account. Bank may stipulate additional NWC if available NWC and anticipated internal accruals are not enough to maintain desired current ratio.

(ii) Suppliers's credit based on market practice

(iii) Other current liabilities like salary payable, advance from customers etc.

(iv) Bank Finance

Calculation of Bank Finance

This method was suggested by Tandon Committee. Though banks have been given complete discretion in this regard, yet banks still follow this method.

There are three methods of lending.

1. As per first method of Tandon Committee, permissible bank finance is equal to 75% of the working capital gap. Working capital gap is equal to total current assets minus current liabilities other than bank borrowing. Borrower's margin will be 25% of the working capital gap. This method will give a current ratio of minimum 1.17:1.
2. As per second method of Tandon Committee, permissible bank finance is equal to 75% of the current assets minus 100% of current liabilities other than bank borrowing. Borrower's margin will be 25% of the current assets. This method will give current ratio of minimum 1.33:1.
3. As per third method, borrower is required to bring 100% of core current assets and at least 25% of the

remaining current assets as margin.

4. If the borrower is not able to bring required margin, he may be given working capital term loan. Thus, working capital term loan was suggested by Tandon Committee.

Cash Budget Method

In any economic activity there will be outflows to meet the expenses of production and inflows from the sale of output. Any firm requires working capital from the bank to meet the gap between these inflows and outflows. Therefore, under this method, cash flows are projected on monthly or quarterly basis to ascertain the deficit. Bank finance will be equal to cash deficit. This method is used while financing seasonal industries like tea, sugar, service oriented industries like software, Non banking finance companies, construction contracts. **Turnover Method:**

6. This method was suggested by Nayak Committee.

7. This method is to be applied in the case of working capital limits up to Rs 5 crore in the case of Small Manufacturing enterprises and up to Rs 2 crore in other cases.

8. This method is simple in nature. According to this method, working capital requirement is equal to 25% of the accepted projected annual sales; bank finance is 20% of the projected annual sales or 80% of the working capital requirements and margin is 5% of the projected annual sales or 20% of the working capital requirements. For example, if the current sales are Rs 400 lac, projected growth is 25%, then projected annual sale will be Rs 500 lac. Accordingly, working capital requirement will be Rs 125 lac, bank finance Rs 100 lac and borrower's margin Rs 25 lac. However, actual drawing power will be allowed as per security available.

9. if net working capital available with the borrower (i.e. borrower's margin) is more than 5% of the projected annual sale, the limits can be adjusted accordingly.

10. The requirement as per this method is minimum assuming working capital cycle of the unit at 3 months. If

working capital cycle is more, Bank may consider higher requirement depending on the business of the borrower.

Turnover Method (Nayak Committee) It is used where the aggregate fund-based working capital credit limits are upto Rs. 500 lac from the banking system.

Working capital : Minimum 25% of the projected turnover (or 3 months's sale).

Working capital limits : Minimum of 20% of projected annual turnover after satisfying about reasonableness of the projected annual turnover. Borrowers' margin : 5% of projected turnover. If it is higher than 5%, the bank limits can be fixed at a lower level than 20%.

The margin proportionately increases with increase in period of operating cycle (ratio *of margin to bank finance should be 1:4.*

Calculation of working capital

Estimated sale turnover (projected sale)	Rs.80 lac
Minimum Working Capital @ 25% estimated sales (which represents 03 months' sales)	Rs.20 lac
Contribution of borrower @ 5%	Rs.4 lac
Minimum Bank credit for working capital @ 20% of projected sales	Rs.16 lac

Traditional method

As per traditional method (Tandon Committee), the level of working capital is determined both by the length of the operating cycle and the size of the sales.

The method is applicable to working capital limits above Rs.5 lac. In a circular dated 04.11.97, RBI withdrew the mandatory application of this method and allowed banks to use their own method.

The total of anticipated level of current assets calculated on the basis of estimated sales and by applying the norms for inventory and receivables, is the level of working capital. The amount of bank limit, can be determined as under :

a: Assess the level of net working capital

(surplus of long term sources over long term uses) available, which normally should not be less than 25% of total current assets.

Work out bank finance to be sanctioned being gap of total current assets less NWC and other current liabilities.

Calculation of limit

Method of lending	1st Method	2"d method
1.Total current assets	2000	2000
2.Less other current liabilities	200	200
capital gap (1-3)	1800	1800
Minimum stipulated NWC	450+	500++
Maximum Permissible Bank Finance	1350	1300

+ Under 1st method it is 25% of working capital gap. ++ Under 2n[d] method it is 25% of total current assets

Bills/Receivable Financing by Banks

Receivable arise on account of sale on credit and are represented as Book Debts or sundry debtors. Finance is provided on the basis of debtors statement provided by the borrower and Drawing power is worked out accordingly. Another method of financing credit sales is Bill financing.

When the borrower makes some sale but not on credit, he issues a deniand bill which is accompanied by document of title to goods like Railway Receipt. If this bill is purchased by bank, funds are provided even up to 100% after deducting charges. The branch of the purchasing bank at purchaser's place presents the bill to the purchaser and releases the document of title to goods against payment.

If the credit is provided on sales, usance bill is drawn on purchaser which is accepted by him. Outstanding amount is shown as Bills Receivable in the books of the seller. In case of such bills, there is increased protection under N I Act as it is Negotiable instrument. Bank provides finance by discounting the bill.

The term 'purchase' is used in case of demand bills, Discount is used for usance bills and negotiation is used when bills are drawn under a Letter of credit. After discounting of bills, it is shown as contingent liability in the books of the drawer i.e. seller.

RBI Guidelines on discounting or rediscounting of bills by Banks

(i) Since banks have already been given freedom to decide their own guidelines for assessing I sanctioning working capital limits of borrowers, they may sanction working capital limits as also bills limit to borrowers after proper appraisal of their credit needs and in accordance with the loan policy as approved by their Board of Directors.

(ii) Banks should clearly lay down a bills discounting policy approved by their Board of Directors, which should be consistent with their policy of sanctioning of working capital limits. In this case, the piocedure for Board approval should include banks' core operating process from the time the bills are tendered till these are realised. Banks may review their core operating processes and simplify the procedure in respect of bills financing. In order to address the often-cited problem of delay in realisation of bilis, banks may take advantage of improved computer / communication networks like the Structured Financial Messaging system (SFMS) and adopt the system of 'value dating' of their clients' accounts.

(iii) Banks should open letters of credit (LCs) and purchase / discount / negotiate bills under LCs only in respect of genuine commercial and trade transactions of their borrower constituents who have been sanctioned regular credit facilities by the banks. Banks should not, therefore, extend fund-based (including bills financing) or non-fund based facilities like opening of LCs, providing guarantees and acceptances to non-constituent borrower or I and non-constituent member of a consortium / multiple banking arrangement. However, in cases where negotiation of bills drawn under LC is restricted to a particular bank, and the beneficiary of the LC is not a constituent of that bank, the bank concerned may negotiate such an LC, subject of the condition that the proceeds will be remitted to the regular banker of the beneficiary. However, the prohibition regarding negotiation of unrestricted LCs of non-constituents will continue to be in force.

(iv) Sometimes, a beneficiary of the LC may want to discount the bills with the LC issuing bank itself. In such cases, banks may discount bills drawn by beneficiary only if the bank has sanctioned regular fund-based credit facilities to the beneficiary. With a view to ensuring that the beneficiary's bank is not deprived of cash flows into its account, the beneficiary should get the bills discounted / negotiated through the bank with whom he is enjoying sanctioned credit facilities.

(v) Bills purchased / discounted / negotiated under LC (where the payment to the beneficiary is not Made 'under reserve') will be treated as an exposure on the LC issuing bank and not on the borrower. All clean negotiations as indicated above will be assigned the risk weight as is normally applicable to inter-bank exposures, for capital adequacy purposes--In the case of negotiations 'under reserve', the exposure should be treated as on the borrower

and risk weight assigned accordingly.

(vi) While purchasing / discounting I—negotiating bills under LCs or otherwise, banks should establish genuineness of underlying transactions / documents.

(vii) The practice of drawing bills of exchange claused 'without recourse' and issuing letters of credit bearing the legend 'without recourse' should be discouraged because such notations deprive the negotiating bank of the right of recourse it has against the drawer under the Negotiable Instruments Act. Banks should not therefore open LCs and purchase / discount / negotiate bills bearing the 'without recourse' clause. On a review it has been decided that banks may negotiate bills drawn under LCs, on 'with recourse 'or 'without recourse 'basis, as per their discretion and based on their perception about the credit worthiness of the LC issuing bank. However, the restriction on purchase/discount of other bills (the bills drawn otherwise than under LC) on 'without recourse 'basis will continue to be in force.

(viii) Accommodation bills should not be purchased / discounted / negotiated by banks. The underlying trade transactions should be clearly identified and a proper record thereof maintained at the branches conducting the bills business.

(ix) Banks should be circumspect while discounting bills drawn by front finance companies set up by large industrial groups on other group companies.

(x) Bills rediscounts should be restricted to usance bills held by other banks. Banks should not rediscount bills, earlier discounted by non-bank financial companies (NBFCs) except in respect of bills arising from sale of light commercial vehicles and two / three wheelers.

(xi) Banks may exercise their commercial judgment in discounting of bills of the services sector. However, while discounting such bills, banks should ensure that actual services are rendered and accommodation bills are not discounted. Services sector bills should not be eligible for rediscounting. Further, providing finance against discounting of services sector bills may be treated as unsecured advance and, therefore, should be within the norm prescribed by the Board of the bank for unsecured exposure limit.

Non fund based working capital timts

BANK GUARANTEE

Bank Guarantees are of three types namely (a) Financial Guarantee (b) Performance Guarantee (c) Deferred Payment Guarantee.

1. Financial Guarantee: When a customer of the bank is required to deposit some amount with court or revenue authority or earnest money and guarantee is issued in lieu of such money, it is called Financial guarantee.

2. Performance Guarantee: This type of guarantees are meant for performance of contracts entered into by the customers.

3. Deferred Payment Guarantee: This type of guarantee is issued when the bank's customer purchases some machine etc on deferred payment basis and that payment is guaranteed by the bank. Following points are to be noted in this regard.

1. Deferred payment guarantee is a type of financial guarantee.

2. Both bank and the purchaser of machinery prefer this type of guarantee as neither is required to part with funds immediately.

3. Basic difference between Term Loan and Deferred Payment Guarantee is on account of outlay of funds. In term loans funds are disbursed immediately whereas in case of DPG, bank is required to make payment when the purchaser of machinery defaults.

4. Appraisal of the DPG proposal is done just like that of a term loan

4. Maximum period for guarantee: Generally maximum period can be up to 10 years. However, banks have been allowed to issue guarantee for more than 10 year also.

5. Liability of Bank: In the case of guarantee, the liability of. bank is contingent liability and it is shown as a footnote to the Balance Sheet.

6. Limitation period in a guarantee: As per amendment to Section 28 of Indian Contract Act, limitation period for enforcing claims under Bank guarantee is 3 years (30 years in case of Govt) from the date of invocation or stipulated expiry date whichever is earlier.

RBI Guidelines on Guarantees

General Guidelines

1. As regards the purpose of the guarantee, as a general rule, the banks should confine themselves to the provision of financial guarantees and exercise due caution with regard to performance guarantee business.
2. No bank guarantee should normally have a maturity of more than 10 years. However, in view of the changed

scenario of the banking industry where banks extend long term loans for periods longer than 10 years for various projects, **RBI** has decided to allow banks to also issue guarantees for periods beyond 10 years.

Precautions for issuing guarantees: Banks should adopt the following precautions while issuing guarantees on behalf of their customers.

1. As a rule, banks should avoid giving unsecured guarantees in large amounts and for medium and long-term periods. They should avoid undue concentration of such unsecured guarantee commitments to particular groups of customers and/or trades.
2. Unsecured guarantees on account of any individual constituent should be limited to a reasonable proportion of the bank's total unsecured guarantees. Guarantees on behalf of an individual should also bear a reasonable proportion to the constituent's equity
3. In exceptional cases, banks may give deferred payment guarantees on an unsecured basis for modest amounts to first class customers who have entered into deferred payment arrangements in consonance with Government policy.
4. Guarantees executed on behalf of any individual constituent, or a group of constituents, should be subject to the prescribed exposure norms.

Precautions for Averting Frauds: While issuing guarantees on behalf of customers, the following safeguards should be observed by banks:

1. At the time of issuing financial guarantees, banks should be satisfied that the customer would be in a position to reimburse the bank in case the bank is required to make payment under the guarantee.
2. In the case of performance guarantee, banks should exercise due caution and have sufficient experience with the customer to satisfy themselves that the customer has the necessary experience, capacity and means to perform the obligations under the contract, and is not likely to commit any default.

3. Banks should refrain from issuing guarantees on behalf of customers who do not enjoy credit facilities with them.

Ghosh Committee Recommendations: In order to prevent unaccounted issue of guarantees, as well as fake guarantees, as suggested by IBA, bank guarantees should be issued in serially numbered security forms. Banks should, while forwarding guarantees, caution the beneficiaries that they should, in their own interest, verify the genuineness of the guarantee with the issuing bank.

Internal Control Systems:

1. Bank guarantees issued for Rs.50,000/- and above should be signed by two officials jointly.

Bank Guarantee Scheme of Government of India

The Bank Guarantee Scheme formulated by the Government of India for the issuance of bank guarantees in favour of Central Government Departments, in lieu of security deposits, etc. by contractors, has been modified from time to time. Under the scheme, it is open to Government Departments to accept freely guarantees, etc. from all scheduled commercial banks. Banks should adopt the Model Form of Bank Guarantee Bond. The Government of India have advised all the Government departments/ Public Sector Undertakings, etc. to accept bank guarantees in the Model Bond and to ensure that alterations/additions to the clauses whenever considered necessary are not one-sided and are made in agreement with the guaranteeing bank. Banks should mention in the guarantee bonds and their correspondence with the

various State Governments, the names of the beneficiary departments and the purposes for which the guarantees are executed. This is necessary to facilitate prompt identification of the guarantees with the concerned departments. In regard to the guarantees furnished by the banks in favour of Government Departments in the name of the President of India, any correspondence thereon should be exchanged with the concerned ministries/ departments and not with the President of India. In respect of guarantees issued in

favour of Directorate General of Supplies and Disposal, the following aspects should be kept in view:

1. In order to speed up the process of verification of the genuineness of the bank guarantee, the name, designation and code numbers of the officer/officers signing the guarantees should be incorporated under the signature(s) of officials signing the bank guarantee.
2. The beneficiary of the bank guarantee should also be advised to invariably obtain the confirmation of the concerned banks about the genuineness of the guarantee issued by them as a measure of safety.
3. The initial period of the bank guarantee issued by banks as a means of security in Directorate General of Supplies and Disposal contract administration would be for a period of six months beyond the original delivery period. Banks may incorporate a suitable clause in their bank guarantee, providing automatic extension of the validity period of the guarantee by 6 months, and also obtain suitable undertaking from the customer at the time of establishing the guarantee to avoid any possible complication later.
4. A clause would be incorporated by Directorate General of Supplies and Disposal (DGS&D) in the tender forms of Directorate General of Supplies and Disposal 229 (Instruction to the tenderers) to the effect that whenever a firm fails to supply the stores within the delivery period of the contract wherein bank guarantee has been furnished, the request for extension for delivery period will automatically be taken as an agreement for getting the bank guarantee extended. Banks should make similar provisions in the bank guarantees for automatic extension of the guarantee period.

Guarantees on Behalf of Share and Stock Brokers/ Commodity Brokers

Banks may issue guarantees on behalf of share and stock brokers in favour of stock exchanges in lieu of security deposit to the extent it is acceptable in the form of bank guarantee as laid down by stock exchanges. Banks may also issue guarantees in lieu of margin requirements as per stock exchange regulations. Banks have further been advised that they should obtain a minimum margin of 50 percent while issuing such guarantees. A minimum cash margin of 25 per cent (within the above margin of 50 per cent) should be maintained in respect of such guarantees issued by banks. The above minimum margin of 50 percent and minimum cash margin requirement of 25 percent (within the margin of 50 percent) will also apply to guarantees issued by banks on behalf of commodity brokers in favour of the national level commodity exchanges, viz., National Commodity & Derivatives Exchange (NCDEX), Multi Commodity Exchange of India Limited (MCX) and National Multi-Commodity Exchange of India Limited (NMCEIL), in lieu of margin requirements as per the commodity exchange regulations. Banks should assess the requirement of each applicant borrower and observe usual and necessary safeguards including the exposure ceilings.

Guarantees favouring Banks: Banks may issue guarantees favouring other banks/ Rs/ other lending agencies for the loans extended by the latter, subject to the condition that the guaranteeing bank should assume a funded exposure of at least 10% of the exposure guaranteed. Banks should not extend guarantees or letters of comfort in favour of overseas lenders including those assignable to overseas lenders. The guarantee issued by the bank will be an exposure on the borrowing entity on whose behalf the guarantee has been issued and will attract appropriate risk weight, as per the extant guidelines.

Payment of invoked guarantees

1. Where guarantees are invoked, payment should be made to the beneficiaries without delay and demur.

2. There should be an effective system to process the guarantee business to ensure that the persons on whose behalf the guarantees are issued will be in a position to perform their obligations in the case of performance guarantees and honour their commitments out of their own resources, as and when needed, in the case of financial guarantees.
3. As per Delhi High Court a bank guarantee is a contract between the beneficiary and the bank. When the beneficiary invokes the bank guarantee and a letter invoking the same is sent in terms of the bank guarantee, it is obligatory on the bank to make payment to the beneficiary.
4. As per Supreme Court, commitment of banks must be honoured.free from interference by the courts and it is only in exceptional cases, that is, to say, in case of fraud or any case where irretrievable injustice would be done if bank guarantee is allowed to be encashed, the court should interfere'.
5. In order to avoid such situations, it is absolutely essential for banks to appraise the proposals for guarantees also with the same diligence, as in the case of fund based limits, and obtain adequate cover by

way of margin so as to prevent the constituents to develop a tendency of defaulting in payments when invoked guarantees are honoured by the banks.

Co-acceptance of bills:

1. While sanctioning co-acceptance limits to their customers, the need therefor should be ascertained, and such limits should be extended only to those customers who enjoy other limits with the bank.
2. Only genuine trade bills should be co-accepted and the banks should ensure that the goods covered by bills co-accepted are actually received in the stock accounts of the borrowers.
3. The valuation of the goods as mentioned in the accompanying invoice should be verified to see that there is no over-valuatioh of stocks.
4. The banks should not extend their co-acceptance to house bills/ accommodation bills drawn by group concerns on one another.
5. The banks discounting such bills, co-accepted by otherbenks, should also ensure that the bills are not accommodation bills and that the co-accepting bank has the capacity to redeem the obligation in case of need.

Co-acceptances in respect of bills for Rs.10,000/- and above should be signed by two officials jointly, deviation being allowed only in exceptional cases, e.g. non-availability of two officials at a branch.

Precautions to be taken in the case of Letters of Credit:

Banks should not extend any non-fund based facilities or additional/ad-hoc credit facilities to parties who are not their regular constituents, nor should they discount bills drawn under LCs, or otherwise, for beneficiaries who are not their regular clients. In the case of LCs for import of goods, banks should be very vigilant while making payment to the overseas suppliers on the basis of shipping documents. They should exercise precaution and care in comparing the clients. The payments should be released to the foreign parties only after ensuing that the documents are strictly in conformity with the terms of the LCs. There have been many irregularities in the conduct of LC business, such as the LC transactions not being recorded in the books of the branch by officials issuing them, the amount of LCs being much in excess of the powers vested in the officials, fraudulent issue of LCs involving a conspiracy/collusion between the beneficiary and the constituent. In such cases, the banks shOuld take action against the concerned officials as well as the constituent on whose behalf the LCs were opened and the beneficiary of LCs, if a criminal conspiracy is involved.

Settlement of claims under Letters of Credits(LCs): In case the bills drawn under LCs are not honoured, it would adversely affect the character of LCs and the relative bills as an accepted means of payment. This could also affect the creditability of the entire payment mechanism through banks and affect the image of the banks. Banks should, therefore, honour their commitments under LCs and make payments promptly.

Factoring: An arrangement between factor and his client, in which atleast, two of the following services are provided by the factor (a) Financing of Receivables (b) Sales Ledger Maintenance (c) Collection of Debts (d) Credit Risk Protection. Factoring is an arrangement in which receivables arising out of sales of goods and services are sold to the factor resulting in the passing of the title to the factor. It is essentially a short-term finance ranging normally between 3 months to 6 months. In India, it was started on the recommendations of the Kalyan Sundram Committee.

Forfaiting: Forfeiting is without recourse discounting of export bills. It is a mechanism of financing of exports a) by discounting export receivable b) evidenced by bill of exchange or promissory note c) without recourse to the seller d) on fixed rate basis (discount) and e) up to hundred percent of the contract value. Forfaiting is done for medium term say between 6 months to 3 years. Before discounting, the bills are avalised by a banker in the importers country who undertakes to make the payment in case payment is not made by the importer.

CERTIFICATE OF DEPOSIT & COMMERCIAL PAPER

	Certificate of Deposit	Commercial Paper
Who can issue	Scheduled commercial banks (except RRBs) and All India Financial Institutions within their 'Umbrella limit'.	Financial Institutions, Primary dealers & reputed companies
CRR/SLR	Applicable on the issue price in case of banks	Not applicable

Investors	Individuals (other than minors),corporations, companies, trusts, funds, associations etc	Individuals (other than minors), corporations, companies, trusts, funds, associations etc.
Maturity	Min: 7 days Max : 12 Months (in case of Fls minimum 1 year and maximum 3 years).	Min: 7 days Max : 12 Months
Amount	Min: Rs.1 lac, beyond which in multiple of Rs.1 lac	Min: Rs.5 lac, beyond which in multiple of Rs.5 lac

Issue of commercial paper by a company : 4 conditions are to be.satisfied (1) Net worth Rs.4 cr, sanctioned working capital, their loan accounts in standard category and credit rating of P2 from CRISIL or equivalent from others.

Features Common to CD & CP

remature cancellation not allowed
ransfer: Endorsement & delivery. Any time
nstrument: Usance Promissory note. Can be issued in Dematerialisation form only
oan : No loan can be given on security of these documents
If payment day is holiday, paid on next preceding business day Issued at a discount to face value

TERM LOANS

Important Points about Term Loans

1. Banks provide term loans normally for acquiring the fixed assets like lad, building, plant and machinery, infrastructure etc., (personal loans, consumption loans, educational loans etc. being exceptions) while the working capital loans are provided for sustaining the working capital i.e. current assets level.
2. In exceptional cases, bank provide term loans for current assets also. This is called working Capital Term Loan (WTCL). If the enterprise is not able to bring in the required amount of NWC, it will feel liquidity crunch and business operations will be affected. In such cases, banks may provide WCTL.
3. Working capital loans are normally sanctioned for one year but are payable on demand. Term loans are payable as per the agreed repayment schedule, which is stipulated in the terms of the sanction. Therefore, for the purpose of matching assets and liabilities of the bank, term loans are considered long term assets while working capital loans are considered as short term assets. Practically, however, an enterprise continues to enjoy the working capital loan till its working is satisfactory, while the term loan gets repaid over a period over a period of time.
4. As a term loan is expected to be repaid out of the future cash flows of the borrower, the DSCR assumes great importance while considering term loans, while for working capital loans, the liquidity ratios assume greater importance.
5. There is no uniform repayment schedule for all terms loans. Each term loan has its own peculiar repayment schedule depending upon the cash surplus of the borrower. Thus, in case of a salaried person, where income level is constant, the repayment can be through EMI system and in case of a farmer, the repayment of principal and interest may coincide with the cropping pattern. In case of industrial enterprises, normally, banks stipulate monthly/quarterly repayment of principal along with all the accumulated interest. In some cases, the entire repayment may be stipulated in one instalment only;called the bullet repayment-.

Deffered Payment Guarantees (DPGs):

1. When the purchaser of a fixed assets does not pay to the supplier immediately, but pays according to an agreed repayment schedule, and the bank guarantees this repayment, the guarantee is called DPG.
2. This is a Non-fund based method for financing purchase of fixed assets.
3. However, if the purchaser defaults in payment o any amount, the bank has to pay the same to the supplier and the exposure becomes fund based till the amount is recovered from the client. The risks involved in a DPG are same as those in a term loan and therefore, the appraisal for a DPG is same as that for a term loan.

Difference between Term Loan Appraisal and Project Appraisal:

(a) In project finance all the financial needs of the enterprise, including working capital requirements, are appraised. This is because the total requirement of long term funds includes margin money for working

capital. After assessing the total requirement of long term funds, the bank decide upon the amount of term loan to be sanctioned and the contribution of the promoters.

If an existing enterprise wants to purchase a few machineries, which are not going to have a major impact on the volume or composition of the business, there is no need for examination of techno-economic feasibility, managerial competence, IRR etc. Bank **will** examine the projections for next 2-3 years to find out that DSCR is at satisfactory level. In case of loans to individuals also, like housing loans, educational loans etc., banks examines the projected DSCR to judge the viability. However, the basic principles of appraisal of a project or a standalone term loan are not different. The appraisal of a standalone term loan proposal is even simpler.

PROJECT APPRAISAL: Project appraisal can be broadly taken in the following steps: (a) Appraisal of Managerial Aspects (b) Technical Appraisal (c) Economic Appraisal

(a) Appraisal of Managerial Aspects: The appraisal of managerial aspects involves examining the following.

1. Credentials of the promoters
2. Financial stake of promoters in the project. Arrangement for bringing additional funds in case of contingencies arising out of delay in project implementation and changes in market conditions.
3. Form of business organization and key persons to be appointed to run the business.

(b) Technical Appraisal: The technical feasibility of a project involves the following aspects: location (ii) products to be manufactured, production process (iii)availability of infrastructure (iv) provider of technology (v) details of proposed construction (vi) contractor for project execution (vii) waste disposal and pollution control (viii) availability of raw materials (ix) marketing arrangements

(c) Economic Appraisal: The economic/financial feasibility of a project involves the following aspects.

(i) Return on Investment: The usual methods used are the NPV, IRR, payback period, cost benefit ratio, accounting rate of return etc.

(ii) Break-even Analysis: A project with a high break-even point is considered more risky compared to the one with lower break-even point.

(iii) Sensitivity Analysis: As market conditions are uncertain, a small change in the prices of raw materials or finished goods may have a drastic impact on the viability of a project. Sensitivity analysis examines such impact.

Appraisal and financing of Infrastructure projects: Infrastructure sector deals with roads, bridges, power, transport, telecommunication, etc. (This is defined in Section 10 of IT Act). Infrastructure projects involve distinct features like exceptionally long implementation, gestation and pay back periods, high debt equity ration etc. While the basic principles of appraisal of an infrastructure project are same as those involved in a normal project appraisal, there are some additional points to be considered.

Types of Financing by In order to meet financial requirements of infrastructure projects, banks may extend credit facility by way of working capital finance, term loan, project loan, subscription to bonds and debentures/preference shares/equity shares acquired as a part of the project finance package which is treated as 'deemed advance' and any other form of funded or non-funded facility.

1. Take-out Financing: Banks may enter into take-out financing arrangement with IDFC/ other financial institutions or avail of liquidity support from IDFC / other FIs.
2. Inter-institutional Guarantees: Banks are permitted to issue guarantees favouring other lending institutions in respect of infrastructure projects, provided the bank issuing the guarantee takes a funded share in the project at least to the extent of 5% of the project cost and undertakes **normal** credit appraisal, monitoring and follow-up of the project.
3. Financing Promoter's Equity: Promoter's contribution towards the equity capital of a company should come from their own resources and the bank should not normally grant advances to take up shares of other companies. In view of the importance attached to the infrastructure sector, it has been decided that, under certain circumstances, an exception may be made to this policy for financing the acquisition promoter's shares in an existing company, which is engaged in implementing or operating an infrastructure project in India. The conditions, subject to which an exception may be made, are as follows:

(i) The bank finance would be only for acquisition of shares of existing companies providing infrastructure facilities as defined in paragraph (a) above. Further, acquisition of such shares should be in respect of companies

where the existing foreign promoters (and/or domestic joint promoters) voluntarily propose to disinvest their majority shares in compliance with SEBI guidelines, where applicable.

(ii) The companies to which loans are extended should, inter alia, have a satisfactory **net worth.**

(iii) The companies financed and the promoters/ directors of such companies should not be a defaulter to banks/Fls.

(iv) In order to ensure that the borrower has a substantial stake in the infrastructure company, bank finance should be restricted to 50 per cent of the finance required for acquiring the promoter's stake in the company being acquired.

(v) Finance extended should be against the security of the assets of the borrowing company or the assets of the company acquired and not against the shares of that company or the company being acquired.

The shares of the borrower company/company being acquired may be accepted as additional security and not as primary security. The security charged to the banks should be marketable.

(vi) Banks should ensure maintenance of stipulated margins at all times.

(vii) The tenor of the bank loans may not be longer than seven years. However, the Boards of banks can Make an exception in specific cases, where necessary, for financial viability of the project.

(viii) This financing would be subject to compliance with the statutory requirements under Section 19(2) of the Banking Regulation Act, 1949.

(ix) The banks financing acquisition of equity shares by promoters should be within the regulatory ceiling of 40 per cent of their net worth as on 31 March of the previous year for the aggregate exposure of the banks to the capital markets in all forms (both fund based and non-fund based).

(x) The proposal for bank finance should have the approval of the Board.

(b) Appraisal

1. In respect of financing of infrastructure projects undertaken by Government owned entities, banks/Financial

Institutions should undertake due diligence on the viability of the project. Banks should ensure that the individual components of financing and returns on the project are well defined and assessed. State government guarantees may not be take as a substitute for satisfactory credit appraisal and such appraisal requirements should not be diluted on the basis of any reported arrangement with the Reserve Bank of India or any bank for regular standing instructions/periodic payment instructions for servicing the loans/bonds.

2. Infrastructure projects are often financed through Special Purpose Vehicles. Financing of these projects would, therefore, call for special appraisal skills on the part of lending agencies. Identification of various project risks, evaluation of risk mitigation through appraisal of project contracts and evaluation of creditworthiness of the contracting entities and their abilities to fulfill contractual obligations will be an integral part of the appraisal exercise. In this connection, banks /Fls may consider constituting appropriate screening committees/special cells for appraisal of credit proposals and monitoring the progress/performance of the projects. Often, the size of the funding requirement would necessitate joint financing by banks/Fls or financing by more than one bank under consortium or syndication arrangements. In such cases, participating banks/Fls may, for the-purpose of their own assessment, refer to the appraisal report prepared by the lead bank/FI or have the project appraised jointly.

Prudential Requirements

Prudential Credit Exposure Limits: Credit exposure to borrowers belonging to a group may exceed the exposure norm of 40 per cent of the bank's capital funds by an additional 10 per cent (i.e. up to 50 per cent), provided the additional credit exposure is on account of extension of credit to infrastructure projects. Credit exposure to single borrower may exceed the exposure norm of 15 per cent of the bank's capital funds by an additional 5 per cent (i.e. up to 20 per cent) provided the additional credit exposure is on account of infrastructure as defined in paragraph (a) above. In addition to the exposure permitted above, banks may, in exceptional circumstances, with the approval of their Boards, consider enhancement of the exposure to a borrower up to a further 5 per cent of capital funds. The bank should make appropriate disclosure in the 'Note on account' to the annual financial statements in respect of the exposures where the bank had exceeded the prudential exposure limits during the year.

2. Assignment of Risk Weight or Capital Adequacy Purposes: Banks are required to be guided by the Prudential Guidelines on Capital Adequacy and Market Discipline-Implementation of the New Capital Adequacy framework, as amended from time to time in the matter of capital adequacy.

3. Asset-Liability Management: The long-term financing of infrastructure projects may lead to asset-liability mismatches, particularly when such financing is not in conformity with the maturity profile of a bank's liabilities. Banks would, therefore, need to exercise due vigil on their asset-liability position to ensure that they do not run into liquidity mismatches on account of lending to such projects.

4. Administrative arrangements: Timely and adequate availability of credit is the pre-requisite for successful implementation of infrastructure projects. Banks/Fls should, therefore, clearly delineate the procedure for approval of loan proposals and suitable monitoring mechanism for reviewing applications pending beyond the specified period. Multiplicity of appraisals by every institution involved in financing, leading to delays, has to be avoided and banks should be prepare to broadly accept technical parameters laid down by leading public financial institutions. Also, setting up a mechanism for an ongoing monitoring of the project implementation will ensure that the credit disbursed is utilized for the purpose for which it was sanctioned.

(d) Take-out Financing/Liquidity Support

1. Take-out Financing Arrangement: Take-out financing structure is essentially a mechanism designed to enable banks to avoid asset-liability maturity mismatches that may arise out of extending long tenor loans to infrastructure projects. Under the arrangements, banks financing the infrastructure projects will have an arrangement with IDFC or any other financial institution for transferring to the latter the out standings in their books on a pre-determined basis. IDFC and SBI have devised different take-out financing structures to suit the requirements of various banks, addressing issues such as liquidity, asset-liability mismatches, limited availability of project appraisal skills, etc. They have also developed a Model Agreement that can be considered for use as a document for specific projects in conjunction with other project loan documents. The agreement between SBI and IDFC could provide a reference point for other banks to enter into somewhat similar arrangements with IDFC or other financial institutions.

2. Liquidity Support from IDFC: As an alternative to take-out financing structure, IDFC and SBI have devised a product, providing liquidity support to banks. Under the scheme, IDFC would commit, at the point of sanction, to refinance the entire outstanding loan (principal + unrecovered interest) or part of the loan, to the bank after an agreed period, say, five years. The credit risk on the project will be take by the bank concerned and not by IDFC. The bank would repay the amount to IDFC with interest as per the terms agreed upon. Since IDFC would be taking a credit risk on the bank, the interest rate to be charged by it on the amount refinanced would depend on the IDFC's risk perception of the bank (in most of the cases, it may be close to IDFC's PLR). The refinance support from IDFC would particularly benefit the banks which have the requisite appraisal skills and initial liquidity to fund the project.

CREDIT DELIVERY

DOCUMENTATION

1. Documents are to be signed by the borrowers and guarantors so that the bank can establish their liability in a court of law.
2. The borrower has to sign the documents which create charge over the primary security, i.e. the security created out of the bank finance.
3. For charge over collateral security, the owner of that security should sign the relevant documents.
4. If the owner of the collateral security is someone other than the borrower, he should first become a guarantor of the loan and then create charge over the security.
5. Each bank's legal department prescribes the standard documents to be taken depending on the type of the loan. In case of a structured loan, the legal department drafts the documents applicable to that particular case.

Precautions in Execution of Documents:

(a) The documents should be properly stamped

(b) The date of execution of documents should never be earlier than the date of stamping. Date and place of execution should be properly mentioned in the documents.

(c) It should be ensured that the parties executing the documents have the necessary authority and the capacity to enter into a contract and executed the documents in that capacity. For example, a partner should sign on behalf of the firm and not in his individual capacity.

(d) It should be ensured that the person signing the documents is doing so with his free will.
(e) The documents should be filled in before these are signed.
(f) In case of companies, the charge should be registered with ROC within 30 days from the date of execution of the documents.
(g) If any document is required to be registered with the Sub-registrar, it should be done within the prescribed time limit.

Third Party Guarantees:

1. Guarantee is taken as an additional safety against default. These third parties can be individuals or any other legal entity.
2. In case of finance to firms, the personal guarantee of proprietor/ partners is not stipulated as they have unlimited liability and their personal assets can be attached for recovery of bank loans.
3. In case of companies and other legal entities, the promoters/ directors/ trustees do not have unlimited/ any liability towards bank's dues. Therefore, in many cases banks stipulate their personal guarantees.

RBI guidelines for personal guarantees of Directors:

1. Personal guarantees of directors may be helpful in respect of companies, whether private or public, where shares are held closely by a person or connected persons or a group (not being professionals or Government), irrespective of other factors, such as financial condition, security available, etc., the exception being in respect of companies where, by court or statutory order, the management of the company is vested in a person or persons, whether called directors or by any other name, who are not required to be elected by the shareholders.
2. Where personal guarantee is considered necessary, the guarantee should preferably be that of the principal members of the group holding shares in the borrowing company rather than that of the director/managerial personnel functioning as director or in any managerial capacity.
3_ Even if a company is not closely held, there may be justification for a personal guarantee of directors to ensure continuity of management or that the changes in management take place with their knowledge.

5. 4. Even where personal guarantees are waived, it may be necessary to obtain an undertaking from the borrowing company that no change in the management would be made without the consent of the lending institution.. Similarly, in the formative stage of a company, guarantee should be obtained to ensure continuity of management. Personal guarantees of directors may be helpful with regard to public limited companies other than those which may be rated as first class, where the advance is on an unsecured basis.
6. There may be public limited companies, whose financial position and/or capacity for cash generation is not satisfactory even though the relevant advances are secured. In such cases, personal guarantee is useful.
7. Cases where there is likely to be delay in creation of charge on assets, guarantee may be taken to cover interim period between the disbursement of loan and creation of charge on assets.
8. The guarantee of parent companies may be obtained in the case of subsidiaries whose own financial condition is not considered satisfactory.
9. Personal guarantees are relevant where the balance sheet or financial statement of a company discloses interlocking of funds between the company and other concerns owned or managed by a group.
10.An undertaking should be obtained from the borrowing company as well as the guarantors that no consideration whether by way of commission, brokerage fees or any other form, would be paid by the former or received by the latter, directly or indirectly. This requirement should be incorporated in the bank's terms and conditions for sanctioning of credit limits. During the periodic inspections, the bank's inspectors should verify that this stipulation has been complied with. There may, however, be an exceptional case where payment of remuneration may be permitted, e.g. where assisted concerns are not doing well and the existing guarantors are no longer connected with the management but continuance of their guarantees is considered essential because the new management's guarantee is either not available or is found inadequate payment of remuneration to guarantors by way of guarantee commission is allowed.

Charge over securities: The type of charge depends upon the nature of security and the operational convenience. Only the owner of an asset can create charge over it. The charge could be any of the following: (a) Mortgage (b) Hypothecation (c) Pledge (d) Lien (e) Assignment.

Possession of Security: Earlier banks favoured `Lock and Key' advances in which the goods are kept in a godown and bank holds the keys of the locks of the godown. However, this system is very inconvenient not only for the

borrower but for the bank also. Therefore, now a days, 'Hypothecation' is preferred, where possession remains with the borrower.

Disbursal of Loans: Working Capital Loans:

Dealing with one or more banks:

1. In case of sole banking, the bank providing working capital limits opens a cash credit account of the borrower and all his financial transactions should be routed through this account.
2. Without bank's permission, no account can be opened with any other bank. Banks give permission to open current account with other bank only if they are convinced about its necessity. in such cases, periodic statements of that account are obtained to keep a tab on the transaction.

Drawing Power:

1. The drawings in the cash credit account are regulated through the system of 'Drawing power' (DP) which is within the sanctioned cash credit limit.
2. Ideally, the DP should be calculated by obtaining a statement of all the current assets and liabilities (excluding outstanding in cash credit account with the bank) and deducting from it the NWC stipulated at the time of assessment of the limit. However, this is not feasible as such a statement is normally available only after accounts are finalized and will be available after much delay and may not serve the purpose.
3. Banks obtain the statement of stocks, book-debts/receivables and the sundry creditors (account payable). These three items form major portion of current assets and liabilities in majority of the enterprises. Drawing power is allowed on fully paid stocks by deducting sundry creditors from stocks and adding sundry debtors.
4. Stock and Debtors statement is normally obtained on monthly basis but the periodicity can be reduced in exceptional cases.
5. By stipulating suitable margins (depending on method of assessment) on stocks and book debts and reducing the amount of sundry creditors, the DP is calculated.

Loan Delivery system

1. Disbursal of entire WC limit by way of cash credit gives wide flexibility to the borrower in his working capital management but, it creates the problem of fund management for the bank as there could be wide fluctuations in the utilization of limits.
2. Cash credit system also offers scope for diversion of funds by the borrower. If the liquidity in the market is tight and short-term interest on money market instruments is high, borrower may tend to utilize the limit fully. In situations of abundant liquidity, the situation is reverse and the utilization of limit may tend to be low. The bank loses in such situations as it has to arrange for short term funds when interest rates are high and is left with surplus funds when rates are low.
3. To meet this situation and to ensure that the utilization of limit is more stable, a portion of sanctioned limit is disbursed by way of 'Loan', which is a fixed component, and remaining amount is disbursed as cash credit. With this, if the borrower wants to draw very little amount or no amount, there will be debit in the loan account (fixed amount) while the cash credit account may have credit balance.

RBI guidelines on Loan Delivery System:

1. In the case of borrowers enjoying working capital credit limits of Rs.10 crore and above from the banking system, the loan component should normally be 80 percent. Banks, however, have the freedom to change the composition of working capital by increasing the cash credit component beyond 20 percent or to increase the 'Loan Component' beyond 80 percent, as the case may be.
2. In the case of borrowers enjoying working capital credit limit of less than Rs.10 crore, banks may persuade them to go in for the 'Loan System' by offering an incentive in the form of lower rate of interest on the loan component, as compared to the cash credit component.
3. In respect of certain business activities, which are cyclical and seasonal is nature or have inherent volatility, the banks may exempt such activities from the loan system of delivery.

Term loans

1. If the term loan is to be disbursed in one go, e.g. purchase of a machine/ ready house, the borrower is asked to deposit his margin with the bank, his loan account is debited by the amount of the loan and the entire amount to be paid to the buyer, is remitted to him by the bank. If any amount has already been paid to the buyer by the customer, satisfactory proof, like details of bank account etc, of this payment is obtained, and this is considered to be a part of his contribution (margin). In exceptional cases, like personal loans or consumption loans, the amount may be credited to

the account of the customer with the bank.

2. In case where the execution of the project is spread over a period of time, the disbursement is normally related to the progress of the project. Therefore promoters may bring contribution in any of these methods:

1. Promoters bring their entire contribution upfront before the bank starts disbursing its commitment.
2. Promoters bring certain percentage of their equity (40%-50%) upfront and balance is brought in stages.
3. Promoters agree, ab initio, that they will bring in equity funds proportionately as the banks finance the debt portion.

The last method has greater equity funding risk. In order to contain this risk, banks should have a clear policy regarding the Debt Equity Ratio (DER) and to ensure that the infusion of equity/fund by promoters should be such that the stipulated level of DER is maintained at all times. Further they may adopt funding sequences so that possibility of equity funding by banks is obviated.

Lending under Consortium/ Multiple Banking Arrangements:

1. The sole banking is suitable for financing working capital needs of an enterprise only if the requirement is within the policy framework of the financing bank. If the requirements grow beyond the comfort level of that bank due to prudential norms or risk perception for a particular segment/borrower, if would like another bank to finance a part of the requirements of that enterprise.
2. If two or more banks get into a formai arrangement to finance the working capital needs of a borrower, it is called consortium arrangement. The consortium banks decide on one of the members as 'Lead bank' who not only arranges periodic meetings of the member banks but also takes lead in assessment, documentation, charge creation, monitoring of the account, etc.
3. In case of multiple banking there is no formal arrangement between the banks though they may share the information about the account in their mutual interest.

RBI Guidelines on Consortium:

1. Various regulatory prescriptions regarding conduct of consortium/multiple banking/syndicate arrangements were withdrawn by Reserve Bank of India in October 1996 with a view to introducing flexibility in the credit delivery system and to facilitate smooth flow of credit. However, as suggested by Central Vigilance Commission, RBI has advised the banks to strengthen their information back-up about the borrowers enjoying credit facilities from multiple banks as follows:

(a) At the time of granting fresh facilities, banks, may obtain declaration from the borrowers about the credit facilities already enjoyed by them from other banks in the format prescribed. In the case of existing lenders, all the banks may seek a declaration from their existing borrowers, availing credit facilities from other banks, and introduce a system of exchange of information with other banks as indicated above.

(b) Subsequently, banks should exchange information about the conduct of the borrowers accounts with other banks at least at quarterly intervals.

(c) Obtain regular certification by a professional, preferably a Company Secretary, Chartered Accountant or Cost Accountant, regarding compliance of various statutory prescriptions that are in vogue.

(d) Make greater use of credit reports available from CIBIL.

(e) The banks should incorporate suitable clauses in the loan agreements in future (at the time of next renewal in the case of existing facilities) regarding exchange of credit information so as to address confidentiality issues.

SYNDICATION OF LOANS: The term 'Syndication' is normally used for sharing a long-term loan to a borrower by two or more banks. This is a way of sharing the risk, associated with lending to that borrower, by the banks and is generally used for large loans. The borrower, intending to avail the desired amount of loan, gives a mandate to one bank (called Lead bank) to arrange for sanctions for the total amount, on its behalf. The lead bank approaches various banks with the details. These banks appraise the proposal as per their policies and risk appetite and take the decision. The lead bank does the liaison work and common terms and conditions of sanction may be agreed in a meeting of participating banks, arranged by the lead bank. Normally, the lead bank charges 'Syndication fee' from the borrower.

CREDIT CONTROL & MONITORING

Credit control and monitoring, often referred as Loan Review Mechanism (LRM), plays an important role in the following aspects:

(a) To ensure that the funds provided by the bank are put to the intended use and continue to be used properly Any diversion of bank's funds out of the business or for unauthorized use within the business should be detected and stopped.

(b) To ascertain that the business continues to run on the projected lines. If there is any deterioration from what was projected at the time of appraisal, the same should be noticed and appropriate action initiated by the bank, in consultation with the borrower, to ensure that the business continues to run on viable lines.

(c) if the deterioration of the business continues despite appropriate action, the bank should decide if any harsh action like, recalling the advance or seizing the security, etc. is necessary. In such cases an early detection of the problem is very important as any delay in necessary action by the bank may result in deterioration of the available security and reduce the chances and amount of recovery.

Tools for Credit Monitoring

(a) Conduct of the Accounts with the Bank: This gives very useful information about the financial health of the enterprise and use of the funds by it. Frequent overdrawings, return of cheques/bills, delays in submission of stock/receivables statements, low turnover, routing of transactions with some other bank, delay in payment of interest/ instalments, devolvement of LCs, invocation of Bank Guarantees, etc. are some of the unsatisfactory features. In such cases, banks may strengthen their monitoring system by resorting to more frequent inspections of borrowers' godowns, ensuring that sale proceeds are routed through the borrower's accounts maintained with the bank and insisting on pledge of the stock in place of hypothecation.

(b) Periodic Information Submitted as per the Terms of the Advance: The statements of stock and receivables are to be submitted by the borrower at regular intervals (normally, monthly) and the bank calculates the Drawing Power (DP) on the basis of these. A thorough scrutiny of these is necessary to verify their correctness, accumulation of inventory (non-moving stocks) and old receivables (normally receivable above six months are exclude for calculating DP). The detection of non-moving stocks and old receivables is not only necessary for correct calculation of DP but is also warranted to detect the danger signals in the business of the borrower. During periodic inspection of the enterprise, by the bank officials, the latest stocks/receivables statement are cross checked with the records. Stocks are also physically verified either fully or on random selection basis:

(c) Stock/Receivables Audit Conducted by the Bank: Stock audit is used by the bank in case of medium and large size accounts where verifying the stocks during normal inspection is not feasible or where the stocks are located at various locations. Similarly, audit of receivables any also be conducted in some cases. The purpose of these audits is to cross check the reliability of the statements_submitted by the borrower.

(d) Financial Statements of the Business, Auditors' Report: These are normally available once a year. An analysis of these statements gives information about the use/diversion of funds, financial health, realization of debts, profitability, etc. In case of working capital limits, this analysis is a part of the renewal exercise.

(e) Periodic Visits and Inspections: (i) it gives an impression about the activity level. The assessment of limits is based on an anticipated level of operations and field visit helps in ascertaining whether activities are at that level or not. (ii) it helps in finding out the position of stocks and other assets charged to the bank (iii) The fact of bank's charge over the assets should be prominently displayed. Field visits help in finding out this.

(f) Interaction with select creditors and debtors.

(g) Periodic secutiny of borrowers' books of accounts and the accounts maintained with other banks.

(h) Market Reports about the Borrower and the Business Segment: These reports are available from the industry associations and rating agencies.

(i) Appointment of Bank's Nominee on Company's Board: In exceptional cases, or in case of large limits, bank may opt to appoint nominee director on the board to keep a tab on the important decisions.

(j) Credit Audit:

Credit Audit

1. Credit audit is an examination of various credit functions of the bank.
2. Credit Audit is normally conducted by internal staff having adequate credit experience.
3. Credit Audit examines compliance with extant sanction and post-sanction processes/procedures laid down by the bank from time to time. Each bank formulates its own policies, procedures, and organizational set up for credit audit.
4. In some banks, credit audit plays an important role in monitoring of large value accounts also.

RBI Guidelines on Credit Audit Objectives of Credit Audit

1. Improvement in the quality of credit portfolio
2. Review sanction process and compliance status of large loans
3. Feedback on regulatory compliance
4. Independent review of Credit Risk Assessment
5. Pick-up early warning signals and suggest remedial measures
6. Recommend corrective action to improve credit quality, credit administration and credit skills of staff, etc. -

Structure of Credit Audit Department: The credit audit/loan review mechanism may be assigned to a specific

Department or the Inspection and Audit Department.

Functions of Credit Audit Department

1. To process Credit Audit Reports
2. To analyse Credit Audit findings and advise the departments/functionaries concerned
3. To follow up with controlling authorities
4. To apprise the Top Management
5. To process the responses received and arrange for closure of the relative Credit Audit Reports
6. To maintain database of advances subjected to Credit Audit

Scope and Coverage: The focus of credit audit needs to be broadened from the account level to look at the overall portfolio and the credit process being followed. The important areas are:

1. Portfolio Review: Examine the quality of Credit & Investment (Quasi Credit) Portfolio and suggest measures for improvement, including reduction of concentrations in certain sectors to levels indicated in the loan policy and Prudential Limits suggested by RBI.

2. Loan Review: Review of the sanction process and status of post sanction processes/procedures (not just restricted to large accounts)

- all fresh proposals and proposals for renewal of limits (within 3-6 months from date of sanction)
- all existing accounts with sanction limits equal to or above a cut off depending upon the size of activity
- randomly selected (say 5-10%) proposals from the rest of the portfolio
- accounts of sister concerns/group/associate concerns of above accounts, even if limit is less that the cut off

3. Action Points for Review

- Verify compliance of bank's laid down policies and regulatory compliance with regard to sanction
- Examine adequacy of documentation
- Conduct the credit risk assessment
- Examine the conduct of account and follow up looked at by line functionaries
- Oversee action taken by line functionaries in respect of serious irregularities
- Detect early warning signals and suggest remedial measures thereof

4. Frequency of Review: The frequency of review should vary depending on the magnitude of risk (say, for the high risk accounts- 3 months, for the average risk accounts — 6 months, for the low risk accounts- **1** year).

- Feedback on general regulatory compliance
- Examine adequacy of policies, procedures and practices
- Review the Credit Risk Assessment methodology
- Examine reporting system and exceptions thereof
- Recommend corrective action for credit administration and credit skills of staff
- Forecast likely happenings in the near future

5. Procedure to be followed for Credit Audit

- Credit Audit is conducted on site, i.e. at the branch which has appraised the advance and where the main operative credit limits are made available.
- Report on conduct of accounts of allocated limits are to be called from the corresponding branches.
- Credit auditors are not required to visit borrowers' factory/office premises.

CREDIT RISK MANAGEMENT & CREDIT RATING

CREDIT RISK

The credit risk can be defined as the unwillingness or inability of a customer or counterparty (e.g. the LC opening bank in a bills negotiation transaction under that LC) to meet his commitment relating to a financial transaction with the bank. For example, in a fund based limit, the credit risk is the non payment of principal and interest by the borrower, as per the agreed terms of repayment. In case of non fund based limit, credit risk arises due to invocation of a guarantee or devolvement of an LC.

Factor affecting credit risk:

(a) External Factors: These factors affect the business of a customer and reduce his capability to honour the terms of financial transaction with the bank. The main external factors affecting the overall quality of the credit portfolio of a bank are, exchange rate and interest rate fluctuations, Government policies, protectionist policies of other countries, political risks, etc. These factors look similar to market risk. But, whereas the market risks directly affect a bank, the factors mentioned here affect the business of the customers thus impairing the quality of the credit portfolio.

Internal Factors: These factors mainly relate to overexposure (concentration) of credit to a particular segment/geographical region, excessive lending to cyclical industries, ignoring purpose of loan, faulty loan and repayment structuring, deficiencies in the loan policy of the bank, low quality of credit appraisal and monitoring, and lack of an efficient recovery machinery.

Steps taken to mitigate credit risks: The major objective of credit risk management is to limit the risk within acceptable level and maximize the risk adjusted rate of return on the credit portfolio. Following are the main steps taken by any bank in this direction:

At macro Level:

1. The risks to the overall credit portfolio of the bank are mitigated through frequent reviews of norms and fixing internal limits for aggregate commitments to specific sectors of the industry/business so that the exposures are evenly spread over various sectors and the likely loss is retained within tolerable limits.
2. Bank also periodically reviews the loan policies relating to exposure norms to single and group borrowers as also the structure of discretionary powers vested with various functionaries.
3. Many banks classify their credit portfolio based on some parameters of quality and periodically review this to avoid any rude shocks relating to credit losses.
4. Normally, banks also formulate policies relating to rehabilitation, compromise, recovery and write off to get the best out of a worst case scenario. At Micro level:
1. This pertains to policies of the bank regarding appraisal standards, sanctioning and delivering process, monitoring and review of individual proposals/categories of proposals, obtention of collateral security etc.
2. Credit ratings and credit scoring play important role in this area.
3. For dispersion/ transfer of risk in large value accounts, bank can resort to consortium/ multiple banking and use of derivatives like credit default swaps.

Credit Ratings: The level of credit risk involved in each loan proposal depends on the unique features of that proposal. Two similar projects, with different promoters, may be appraised by a bank as having different credit risks. Similarly, Two different projects, with same promoters, may also be appraised by the bank as having different credit risks. While appraising a credit proposal, the risk involved is also measured and often quantified by way of a rating.

Objective of Credit Rating:

(a) To decide about accepting, rejecting or accepting with modifications/ special covenants
(b) To determine the pricing, i.e. the rate of interest to be charged
(c) To help in the macro evaluation of the total credit portfolio by classifying it on the ratings allotted to individual accounts. This is used for assessing the provisioning requirements, as also a decision making tool, by the management of the bank, for reviewing the loan policy of the bank.

Internal and External Ratings: Most ofthe bank's in India have set up their own credit rating models. Some of the outside credit rating agencies are: CARE, ICRA, CRISIL and SMERA.

Methodology of Credit Rating: Based its on loan policies and risk perception, each bank has its own rating model. Common feature in all the risk models is that a score is given for different perceived risks by allotting different weightages. The sum of all these scores forms the basis for deciding on risk rating of a proposal. Normally, the broad categories of risk areas which are scored, are:

(a) Promoters/Management aspects and the securities available
(b) Financial aspects based on analysis of financial statements
(c) Business/project risks

In view of the dynamic market scenario, there is need to review the ratings of a borrower at regular intervals upgrade or downgrade or maintain it. —

Use of Credit Derivatives for-Risk Management:

1. Credit derivatives are used to hedge the risks inherent in any credit asset without transferring the asset itself.
2. The hedging is comparable to insurance and comes at a cost. Therefore, if the anticipated risk does not materialize, the return from the asset will be less than what it would have been without the hedging.
3. While simple techniques for transferring credit-risk, such as financial guarantees, collateral and credit insurance have been prevalent in the Indian banking industry for long, the recent innovative instruments in credit risk transfer (CRT) such as collateralized debt obligations (CDO), etc. are yet to gain significant currency.
4. Credit Default Swaps (CDSs) finds use as the new hedging instrument.

Credit Default Swaps (CDSs):

1. This is a bilateral contract in which the risk seller (lending bank) pays a premium to the buyer for protection against credit default or any other specified credit event.
2. Normally, CDS is a standardized instrument of ISDA (International Swaps and Derivatives Association).
3. The credit events defined by ISDA are, bankruptcy, failure to pay, restructuring, obligation acceleration, obligation repudiation/ moratorium etc_

4. As per RBI guidelines, only plain vanilla CDSs are allowed.

Credit Linked Notes (CLN):

1. In this, the risk seller gets risk protection by paying regular premium to the risk buyer, which is normally a SPV which issued notes linked to the underlying credit. These notes are purchased by the general investors and the money received from them is used by the SPV to buy high quality securities. The general investors get fixed or variable return on the note during its life. In maturity of the underlying credit, the securities purchased by SPV are sold and money returned to the investors. But, in case of default.in the underlying credit, these securities are used to pay to the risk seller.

Concern about Derivatives:

If the banks use these derivatives to hedge their credit risk by way of purchasing the risk protection, there is no apprehension. But, when the banks start selling the credit protection to other lenders, in respect of their credit risks, there is cause for worry because, often these instruments are so structured that they become very complex to understand and sometimes the liability which arises is many times more than what was anticipated. Therefore, RBI is in favour of slow growth of these derivatives in Indian financial market. As per Warren Buffet, the famous investor, 'These are weapons of mass financial destruction'.

BASEL II ACCORD:

The new framework of Basel II accord is based on three pillars viz., i) Minimum capital requirements, ii) Supervisory review and iii) Market discipline. The minimum capital requirement is based on market risk, operational risk and the credit risk. Basel II hag laid down various approaches for assessment of credit risks. These are: Standardised Approach (ii) Foundation Internal Rating Based (IRB) Approach (iii) Advanced Internal Rating Based (IRB) Approach. Foreign banks operating in India and Indian banks having operational presence outside India have migrated to the simpler approaches available under the Basel II Framework, since March 31, 2008. Other commercial banks have also migrated to these approaches from March 31, 2009. Thus, the Standardised Approach for credit risk has been implemented for the bank in India.

Introduction of Advanced Approaches of BASEL II Framework in India:

Having regard to the necessary up-gradation of risk management framework as also capital efficiency likely to accrue to the banks by adoption of the advanced approaches envisaged under the Basel II Framework and the emerging international trend in this regard, RBI considered it desirable to lay down a timeframe for

implementation of the advanced approaches in India. This would enable the banks to plan and prepare for their migration to the advanced approaches for credit risk. RBI has advised the following time schedule for implementation of the advanced approaches (Foundation as well as Advanced IRB approach);

I. The earliest date of making application by banks to RBI — April 1, 2012

2. Likely date of approval by the RBI — March 31, 2014

RBI has advised the banks to undertake an internal assessment of their preparedness for migration to advanced approaches, in the light of the criteria envisaged in the Basel II document, as per the aforesaid time schedule, and take a decision, with the approval of their Boards, whether they would like to migrate to any of the advanced approaches. The banks deciding to migrate to the advanced approaches may approach RBI for necessary approvals, in due course, as per the stipulated time schedule. lf, the result of a bank's internal assessment indicates that it is not in a position to apply for implementation of advance approach by the above mentioned dates, it may choose a later suitable to it based upon its preparation. The banks, at their discretion, have the option of adopting the advanced approaches for one or more of the risk categories, as per their preparedness, while continuing with the simpler approaches for other risk categories, and it would not be necessary to adopt the advanced approaches for all the risk categories simultaneously. However, the banks should invariably obtain prior approval of the RBI for adopting any of the advanced approaches.

REHABILITATION & RECOVERY

Credit Default/ Stressed Assets/NPAs

Credit default means the inability or the unwillingness of a customer or counterparty to meet commitments in relation to lending, trading, or any financial transactions. This may take the following forms:

(a) in the case of direct lending: principal/ and or interest amount may not be repaid as per the terms of repayment

(b) in the case of guarantees or letters of credit: funds may not be forthcoming from the constituents upon crystallization of the liability;

(c) in the case of treasury operations: the payment or series of payments due from the counter parties under the respective contracts may not be forthcoming or ceases;

(d) in the case of securities trading businesses: funds/securities settlement may not be effected;

(e) in the case of cross-border exposure: the availability and free transfer of foreign currency funds may either cease or restrictions may be imposed by the sovereign.

Stressed assets are those assets in which the default has either already occurred or which are facing a reasonably certain prospect of default. For example, the term loan for an industrial project, implementation of which has been abandoned, is a stressed asset even though the repayment has not yet fallen due as per the repayment terms.

Wilful Defaulters

The committee on Wilful Defaulters was headed by Shri S.S. Kohli.

What is a willful default: A "wilful default" would be deemed to have occurred if case of following events:

1. The unit has defaulted in meeting its payment / repayment obligations to the lender even when it has the capacity to honour the said obligations.

2. The unit has defaulted in meeting its payment / repayment obligations to the lender and has not utilised the . finance from the lender for the specific purposes for which finance was availed of but has diverted the funds for other purposes.

3. The unit has defaulted in meeting its payment / repayment obligations to the lender and has siphoned off the funds so that the funds have not been utilised for the specific purpose for which finance was_availed of, nor are the funds available with the unit in the form of other assets.

4. The unit has defaulted in meeting its payment / repayment obligations to the lender and has also disposed off or removed the movable fixed assets or immovable property given by him or it for the purpose of securing a term loan without the knowledge of the bank/lender. The default to be categorised as wilful must be intentional, deliberate and calculated.

Reporting to CIBIL : Where suits have been filed: Bank/Fls should submit the list of suit-filed accounts of wilful defaulters of Rs.25 lakh and above as at end-March, June, September and December every year to CIBIL. Reporting to RBI: Where suits have not been filed: Banks/Fls should, submit the quarterly list of wilful _defaulters where suits have not been filed only to RBI. Banks need not report cases where (i)outstanding amount falls below Rs.25 lakh and (ii) in respect of cases where banks have agreed for a compromise settlement and the borrower has fully paid the

compromised amount.

Grievances Redressal Mechanism : (1) With a view to imparting more objectivity in identifying cases of wilful default, decisions to classify the borrower as wilful defaulter should be entrusted to a Committee of higher functionaries headed by the Executive Director and consisting of two GMs/DGMs as decided by the Board of the concerned bank/Fl. (ii) The borrower should be provided opportunity to make representation against such decision to a Grievance Redressal Committee headed by the Chairman and Managing Director and consisting of two other senior officials. A final declaration as 'wilful defaulter' should be made after a view is taken by the Committee on the representation and the borrower should be suitably advised.

Options available to Banks for Stressed Assets: Normally, a bank follows the following steps in case of a stressed asset: Exit from the account (b) Rescheduling/ Restructuring (c) Rehabilitation (d) Compromise (e) Legal action (f) Write off

(a) Exit from the Account: Exit from an account is possible only when the symptoms of stress are detected at a very early stage so that the borrower is able to shift his account to another bank which has a different credit appetite. Once the symptoms become more pronounced, acceptance of account by another bank may not materialize. In case of consortium/multiple banking, there is good possibility of other banks taking up the share of the bank wanting to exit.

(b) Reschedulino/Restructuring: If the default is not willful, the banks normally reschedule or restructure the loans in accordance with the revised cash flow estimates of the borrower.

(c) Rehabilitation: Sometimes, the business enterprises face adverse internal or market conditions and incur losses for a long time, resulting in default in payment of bank's dues. This is specially true of the manufacturing enterprises. Banks may examine the possibility of 'Rehabilitation' in such cases after undertaking detailed viability study.

(d) Compromise: If the restructuring/ rescheduling/ rehabilitation is not considered viable or, does not yield the desired results, banks try to recover their dues by offering some concessions to the borrower. Such decision is influenced by the availability/ realisability of the securities, enforceability of the documents etc.

(e) Legal Action: In cases where event the compromise does not materialize, banks have to initiate recovery proceedings. The forums available to the banks are as under:

(0 Government Machinery: In case of finance under government sponsored schemes, the recovery
officers, appointed by the state governments, help in recovery of bank's dues

(ii) Civil Courts: Banks can file the civil suits for recovery of their dues in the civil courts. This option is used for dues less than Rs ten lacy only. However, the proceedings in the civil courts are very slow. The CFSA (committee on financial sector assessment) has observed that, 'the average time taken in India for winding-up proceedings is one of the highest in the world. Improvements in effective enforcement of creditor rights and insolvency systems are critical for strengthening market efficiency and integration and for enhancing commercial confidence in contract enforcement.

(iii) Lok Adalats: In the area of dispute settlement, the Legal Services Authority Act, 1987 has conferred statutory basis on the Lok Adalats (people's courts). The Reserve Bank has consequently issued guidelines to commercial banks and financial institutions to make increasing use of the forum of Lok Adalats. Banks could settle disputes involving amounts up to Rs. 20 lakh through the forum of Lok Adalats. Banks can also participate in the Lok Adalats convened by various DRTs/DRATs for resolving cases involving Rs.10 lakh and above.

(iv) Debt Recovery Tribunals (DRTs): These are created specially for banks and Fls for expenditing the recovery cases involving amounts of Rs 10 lakh and above.

(v) SARFAESI Act, 2002:

(f) Write off: When all the efforts to recover the dues- are exhausted or, the bank is convinced that further pursuit of the case will not result any worthwhile results, the outstanding amount is written off by utilizing the provision made for that account in the books. If the provision is not enough, the excess amount is debited to **P &** L account. The write off does not mean that the borrower's liability to the bank has ended. If bank is able to recover any amount from him in future, it has the legal right to appropriate that amount.

Lok Adalats

1. Lok Adalats are created under Legal Services Authority Act 1987
2. There are certain advantages in using the forum of Lok Adalats by banks and financial institutions in compromise settlement of their NPAs. There are no court fees involved when fresh disputes are referred to it. It can

take cognizance of any existing suit in the court as well as look into and adjudicate upon fresh disputes. If no settlement is arrived at, the parties can continue with court proceedings. Its decrees have legal status and are binding.

3. Since its decisions are consent decree, no appeal can be filed against decision of Lok Adalat.

4. Cases involving an amount upto Rs.20 lakh may be referred to Lok Adalats. However, if the Lok Adalat is arranged by DRT, cases involving amount of more than Rs 20 lakh can also be filed

5. In order to make a definite impact on reduction of NPAs, the scheme may include all NPA accounts, both suit filed and non-suit filed accounts, which are in "doubtful" and "loss" category, with outstanding balance up to Rs.20 lakh. No cut off date is suggested since Lok Adalat is an on-going process.

6. Repayment should be preferably by down payment and within a maximum period of Ito 3 years.

7. Civil Procedure Code is applicable and they are civil courts for this purpose.

8. Filing a case with Lok Adalat does not extend limitation period.

Debt Recovery Tribunals

1. DRTs are Special types of courts for effecting recovery of dues of banks and financial institutions.

2. DRTs are established under the Recovery of Debts due to banks and financial institutions Act 1993

3. The Act is not applicable to J&K.

4. DRT is headed by a Presiding Officer. He is assisted by a Recovery Officer and one Registrar.

5. Type of Cases: Cases involving recoverable dues of banks and Fls of Rs 10 lacs and above only are filed with DRTs. Such cases can not be filed in the normal civil courts.

6. Once the case is decided in favour of the bank or FI, the DRT issues a Recovery Certificate. Recovery Officer who has powers such as attachment etc. helps in recovery of dues through execution of the decree passed by DRT.

7. Appeal against the order of the Recovery Officer can be made to DRT within 30 days of passing the order.

8. Any appeal against the judgement of DRT can be preferred with Debt Recovery Appellate Tribunal_ The head of DRAT is called Chairperson. The appeal is made within 45 days of the date of receipt of the order. If borrower wants to appeal, 75% of the judgment amount is required to be deposited which can be waived or reduced by the Chairperson of the DRAT even to nil.

9. Fee: for filing case with DRT- up to Rs 10 lac : Rs 12,000; For each additional Rs **1** lac or part thereof it is Rs 1000. Maximum amount of fees is Rs 1,50,000,

For filing appeal with DRAT- Where the amount of debt is less than Rs 10 lakh- Rs 12,000; For debts due between Rs 10 lakh to less than Rs 30 lakh- Rs 20,000;

For debts of Rs 30 lakh and more — Rs 30,000

10. For being appointed as DRT, a person should qualify to be District Judge and for being appointed as DRAT, the person should qualify to be a Judge of the High Court.

Securitisation, and Reconstruction of Financial Assets and Enforcement of Security Interest Act

1. The Act was passed in 2002 with the objective of helping banks / Fls in recovery of their dues without intervention of the court. The Act is applicable throughout India including Jammu & Kashmir.

2. The Act empowers the secured creditor to (i) take possession of the security (ii) sale or lease or assign the right over the same (iii) Manage the same and/or appoint any person to manage the same (iv) Recover money receivable from 3rd parties. The competent authority to enforce rights under SARFAESI is Chief Manager and above. However, Board of the bank can also delegate authority to an officer below the rank of Chief Manager.

3_ A bank can exercise rights under the Act provided following conditions are satisfied.

(a) The asset to be acquired should be charged to the bank.

(b) The recoverable dues should be more than Rs 1,00,000.

(c) The Act is not applicable if 80% of the Principal has been paid. It means outstanding amount should be more than 20% of the Principal amount.

(d) A notice of 60 days is required to be given to the borrower and guarantor under section 13(2) of the Act calling upon them to discharge the liabilities failing which bank can acquire the assets m

(e) If loan has been raised from more than one bank/Fl, consent of 75% of lenders by value is required before initiating action under the Act

(f) The Act does not cover agricultural land mortgaged to the credit institution. (However, other assets charged to bank can be acquired).
(g) The account should be NPA
(h) The documents are within the limitation period
(i) The security is not charged by pledge or lien

4. The Act was challenged before Supreme Court in the case of Mardia Chemicals Limited versus Union of !ndia and others (ICICI). While upholding the constitutional validity of the Act, the Court struck down a clause that required borrower to deposit 75% of the claim amount before making an appeal before DRT against action of the bank. Accordingly, the Act was revised in 2004 and the revised provisions are given in the subsequent paragraphs.

5. If borrower has objection against the action of the bank, he can object to the bank and bank has to reply within one week. If borrower is still not satisfied he can file application with the DRT within 45 days of the taking over of possession by the bank and is not required to deposit any amount with DRT at this stage. If bank or borrower is not satisfied with the decision of DRT, either party can make appeal to DRAT within 30 days of receiving the copy of judgement. However, if the borrower prefers an appeal with DRAT, he is required to deposit 50% of the bank's claim which can be reduced to 25% by the Chairperson.

6. If the .bank wants to sell the acquired assets, 30 days notice is to be given to the borrower/guarantor. The sale can be made by obtaining quotations or inviting tenders from public or by holding public auction. In case of auctions or tenders reserve price will be fixed by the bank and sale at below reserve price will require consent of the borrower. Sale will be confirmed by bank on receipt of 25% of the amount immediately and balance in 15 days.

7. In the case of Transcore versus Union of India & Others, Supreme Court has decided that bank take action simultaneously under SARFAESI and RDB Act (DRT Act)

Debt Restructuring:

Corporate Debt Restructuring (CDR)

1. CDR was initiated on the recommendations of the Vepa Kamesam Committee. The same was revised in November 2005 on the recommendations of the Special Group headed by Ms Shyamala Gopinath.The revised scheme is given below:

2. Eligibility: (i) The borrower should be a corporate borrower i.e. Companies, Co-operative societies etc. (ii) The loan should have been raised from more than one bank or financial institution. Single lender accounts are not covered. (iii) Outstanding exposure should be Rs.10 crore or more. (iv) The CDR Mechanism is available to the corporates engaged in industrial as well as non-industrial activities. (v) The borrower should not have committed a fraud. (vi) Wilful defaulters can be considered only with consent of Core Group. (vii) The account should be Standard, Sub Standarad or Doubtful. (viii) Loss accounts are not covered.

3. Structure if the CDR system: The CDR structure consists of three tier structure namely (i) CDR Standing Forum and its Core Group (ii) CDR Empowered Group (iii) CDR Cell. CDR Standing Forum is a self-empowered body, which lays down policies and guidelines, and monitor the progress of CDR. The CDR Standing Forum comprise of CMD IDB1, Chairman, State Bank of India; Managing Director & CEO, 1=1 Bank Limited; Chairman, Indian Banks' Association as well as CMDs of all banks and financial institutions participating as permanent members in the system. The CDR Standing Forum shall meet at least once every six months. A CDR Core Group will be carved out of the CDR Standing Forum to assist the Standing Forum. The Core Group will consist of Chief Executives of Industrial Development Bank of India Ltd., State Bank of India, ICICI Bank Ltd, Bank of Baroda, Bank of India, Punjab National Bank, Indian Banks' Association and Deputy Chairman of Indian Banks' Association representing foreign banks in India. ii) CDR Empowered Group consists of ED level representatives of Industrial Development Bank of India Ltd., ICICI Bank Ltd. and State Bank of India as standing members, in addition to ED level representatives of financial institutions and banks who have an exposure to the concerned company. The individual cases of corporate debt restructuring shall be decided by the CDR Empowered Group. iii) CDR Cell will make the initial scrutiny of the proposals received from borrowers / creditors, and put up the matter before the CDR Empowered Group, within one month to decide whether rehabilitation is prima fade feasible.

4. Category I and Category II restructuring: Category I is applicable to Standard and Sub standard

accounts and Category II is applicable to Doubtful category. For making reference under CDR I, consent of 20% of lenders by value is required whereas for making reference of doubtful accounts under CDR II and suit filed accounts, consent of 75% lenders by value and 60% by number is required.

5. Stand still clause: Debtors and creditors agree through an agreement called Debtor Creditor agreement that 'no party shall take legal action during the standstill period i.e. 90 days (can be extended to 180 days).

6. Inter Creditor Agreement: Creditors will enter into legally binding inter creditor agreement which will be valid for 3 years and can be extended by 3 years. They will agree that the decision will be binding on all creditors where 75% of creditors by value and 60% by number agree.

7. Procedure: Preliminary 'case for restructuring will be prepared by the lead institution within one month for submission to CDR cell. CDR cell will prepare restructure plan within 30 days for decision by CDR empowered group within 90 days. The main criteria for decision will be that the unit should be able to become viable in 7 years and restructured debt should be paid within 10 years. Other important aspects for consideration of proposal include return on capital employed, DSCR, gap between internal rate of return and cost of funds and extent of sacrifice.

8. Asset classification: If approved package is implemented within 120 days, then asset classification will be restored to the same as was existing on the date of making reference.

Debt Restructuring Mechanism for SMEs

1. The guidelines are applicable to entities which are viable or potentially viable as follows : (i) All non-corporate SMEs irrespective of the level of dues to banks. (ii) All corporate SMEs which are enjoying banking facilities from a single bank, irrespective of the level of dues to the bank. (iii) All corporate SMEs which have funded and non-funded outstanding up to Rs.10 crore under multiple/ consortium banking arrangement.

2. Accounts involving wilful default, fraud and malfeasance would not be eligible for restructuring. The Reserve Bank has advised that banks may review the reasons for classification of the borrower as wilful defaulter and satisfy themselves that the borrower is in a position to rectify the wilful default provided he is granted an opportunity. Banks may admit such exceptional cases for restructuring with their board of directors' approval. Banks should, however, ensure that cases involving frauds or diversion of funds with malafide intent are not covered.

3. Accounts Classified by banks as Standard, Sub Standad and Doubtful only are covered. "Loss assets" would not be eligible for restructuring.

4. For cases under the purview of the Board for Industrial and Financial Reconstruction (BIFR) banks should ensure completion of all formalities in seeking approval from **BIFR** before implementing the package.

5. Viability: Banks should decide on the acceptable viability benchmark. It should be ensured that the unit becomes viable in 7 years and the repayment period for restructured debt does not exceed 10 years.

6. Additional Finance: Additional finance, if any may be treated as Standard Asset in all accounts namely standard, sub standard and doubtful accounts up to a period of one year after the date when first payment of interest or of principal whichever is earlier falls due under the approved restructuring package. It the restructured asset does not qualify for upgradation at the end of the above period, additional finance shall be placed in the same asset classification category as the restructured debt.

7. Upgradation of restructured accounts: The account would be upgraded to the standard category after one year from the date when first payment of interest or of principal whichever is earlier falls due under the rescheduled terms provided there is a satisfactory performance during the period.

8. Time period for restructuring: Restructuring package should be implemented within a maximum period of 60 days from the date of receipt of request.

RBI guidelines on Rehabilitation of Sick SSI Units:

As per the definition, a unit is considered as sick when any of the borrowal account of the unit remains substandard for more than 6 months or there is erosion in the net worth due to accumulated cash losses to the extent of 50% of its net worth during the previous accounting year and the unit has been in commercial production for at least two years. The criteria will enable banks to detect sickness at an early stage and facilitate corrective action for revival of the unit. As per the guidelines, the rehabilitation package should be fully implemented within six months from the date the unit is declared as potentially viable / viable .During this six months period of identifying and implementing rehabilitation package banks/Fis are required to do "holding operation" which will allow the sick unit to draw funds from the cash credit account at least to the extent of deposit of sale proceeds

Following are broad parameters for grant of relief and concessions for revival of potentially viable sick SSI units:

1. Interest on Working Capital - Interest 1.5% below the prevailing fixed/ prime lending rate, wherever applicable.
2. Funded Interest Term Loan - Interest Free
3. Working Capital Term Loan - Interest to be charged 1.5% below the prevailing fixed / prime lending rate,wherever applicable
4. Term Loan - Concessions in the interest to be given not more than 2 % (not more than 3 % in the

case of tiny / decentralised sector units) below the document rate.

5. Contingency Loan Assistance The Concessional rate allowed for Working Capital Assistance

Credit Information System:

1. The need of credit information system was felt in order to alert the banks and financial institutions (Fis) and put them on guard against borrowers who have defaulted in their dues to other lending institutions. It was

also imperative to arrest accretion of fresh NPAs in the banking system through an efficient system of credit information on borrowers as a first step in credit risk management.

2. A working Group (Chairman: Shri N.H. Siddiqui) had recommended to set up a CIB under the Companies Act, 1956 with equity participation from commercial banks, Fls and NBFCs registered with the Reserve Bank. As per the recommendations made by the Working Group, Credit Information Bureau (India) Ltd., (CIBIL) was set up by state Bank of India in association with HDFC in January 2001.
3. In order to get over the legal constraints of customer confidentially vis-a-vis providing information on banks' customers to CIBIL, pending enactment on the Credit Information Companies (Regulation) Act, the Reserve Bank advised banks and financial institutions on October 1, 2002 to obtain consent from all existing borrowers and guarantors at the time of renewal of loans and consent of all the new borrowers/guarantors for sharing the credit information in respect of non-suit filed accounts with the CIBIL. A Working Group (Chairman: Shri S.RI lyer) set up in 2002 observed that while some modalities like 'consent clause' could be adopted as a base to begin with, for limited operations of a CIB, such modalities cannot be a substitute for a special legislation.
4. The Credit Information Companies (Regulation) Act, 2005 was passed in May 2005. In terms of section 15(1) of the Act, every credit institution has to become member of at least one credit information company with a period of three months from commencement of the Act or any extended time allowed by the Reserve Bank on application. As per RBI guidelines, each credit institution should provide credit data (positive as well as negative) to the credit information company in the format prescribed by the credit information company.
5. As per Section 21(1) of the Credit Information Companies (Regulation) Act, 2005, 'any person, who applies for grant or sanction of credit facility, from any credit institution, may request such institution to furnish him a copy of the credit information obtained by such institution from the credit information company. Every credit institution shall on receipt of request, furnish to such person a copy of the credit information subject to payment of charges specified by the Reserve Bank. RBI has prescribed a maximum fee of Rs.50/- (Rupees fifty only) for the purpose.

Credit Information Bureau of India Ltd (CIBIL):

CIBIL was set up by State Bank of India in association with HDFC in January 2001. Presently, Later on other banks also joined as equity holders. Besides CIBIL, RBI has issued certificate of registration to three more companies to work as Credit Information Company. These companies are: Experian Credit Information Company of India Private Ltd., Equifax Credit Information Services Private Ltd., High Mark Credit Information Services Private Limited. The purpose of setting up of CIBIL and other information companies is information sharing on defaulters as also other borrowers as comprehensive credit information, which provides details pertaining to credit facilities already availed of by a borrower as well as his payment track record, has become the need of the hour,

CIBIL's aim is to fulfill the need of credit granting institutions for comprehensive credit information by collecting, collating and disseminating credit information pertaining to both commercial and consumer borrowers, to a closed user group of Members. Banks, Financial Institutions, Non banking Financial Companies, Housing Finance Companies and Credit Card Companies use CIBIL's services. Data sharing is based on the Principle of Reciprocity, which means that only Members who have submitted all their credit data, may access Credit Information Reports from CIBIL. The relationship between CIBIL. And its Members is that of close interdependence.

RBI/CIBIL disseminate information on non-suit filed and suit filed accounts respectively, as reported to them by the banks/Fls and responsibility for reporting correct information and also accuracy facts and figures rests with the concerned banks and financial institutions. Therefore, RBI has advised the banks and financial institutions to take immediate steps to up-date their records and ensure that the names of current directors and reported. In addition to reporting the names of current directors, it is necessary to furnish information about directors who were associated with the company at the time the account was classified as defaulter, to put the other banks and financial institutions on guard. Banks and Fis may also ensure the acts about directors, wherever possible, by cross-checking with Registrar of Companies.

As per RBI guidelines, bank/Fls are required to submit the list of suit-field accounts of willful defaulters of Rs.25 lakh and above as at end-March, June, September and December every year to Credit Information Bureau (India) Ltd. The data on borrowal accounts against which suits have been filed for recovery of advances (outstanding aggregating Rs.1.00 crore and above) and suit filed accounts of willful defaulters with outstanding balance of Rs.25 lakh and above, based on information furnished by scheduled commercial banks and financial institutions is available at website of CIBIL.

MODULE – D : CREDIT MANAGEMENT

TEST YOURSELF NO. : 1

1. As per RBI guidelines, the turnover method of assessment should be applied for working capital limits of up to Rs in case of SSI units.

(a) One Crore (b) Two Crore (c) Five Crore (d) Ten Crore

2. Interest rates, regulated by RBI, are applicable for credit limits up to Rs. _____ lakh

(a) One (b) Two (c) Five (d) Ten *(e) None of these

3. The total priority sector target for foreign banks, operating in India, with less than 20 branches is% of ANBC or credit equivalent of Off Balance Sheet Exposure whichever is higher.

(a) 20% *(b) 32% (c) 40% (d) 18%

4. Net working capital meas which of the following?

(a) Total current assets minus bank finance

(b) Total current assets minus credit from suppliers

*(c) Total current assets minus total current liabilities

(d) Short term sources brought in by promoters

5. Which of the following statements is not true for efficient inventory management?

(a) It results in reduction in inventory

(b) It reduces the working capital requirements of the enterprise. *(c)

It reduces the NWC available with the enterprise.

(d) It increases the Inventory Turnover Ratio if the level of sales remains the same.

6. Which of the following is not a source for meeting working capital requirements?

(a) Suppliers Credit (b) Bank Finance (c) Other current liabilities *(d) Advance payment to suppliers

7. Which of the following is a liquidity ratio?

*(a) Quick Ratio (b) TOLITNW (c) DSCR (d) DER

8. Which of the following is not correct regarding Current Ratio?

(a) For same level of current assets, increase in NWC results in increased current ratio.

(b) The current ratio can be less than one

*(c) The current ratio can be negative.

(d) Current ratio is an indicator of liquidity.

9. The commercial paper can be issued by which of the following?

*(a) Corporates (b) Corporates and partnership firms (c) Any Business Entity (d) None

10.Which of the following is not correct regarding forfeiting?

(a) It is a form of working capital finance

(b) It is used in export finance

*(c) It is with recourse to the drawer of the bill.

(d) Under this financier discounts the bills drawn on buyer.

11.Which of the following is correct regarding Letters of Credit?
(a) These are opened by a bank for export sales by the client
(b) These are opened by a bank for local sales by the client.
(c) Letters of Credit do not carry much risk for the opening bank.
*(d) Letters of Credit are opened by a bank for purchase of goods by' the client.
12.Under Turnover method of assessment, the limit is sanctioned at per Cent of the projected turnover.
(a) 25 *(b) 20 (c) 30 (d) 35
13. Cash Budget Method of assessment is more suitable for those business enterprises which have
(a) uniform level of operations (b) High level of operations
(c) Low level of operations *(d) Seasonal Operations
14.A DPG is issued by the bank for _____ , by its client
(a) Sale of goods (b) Purchase of goods
(c) Sale of capital goods *(d) Purchase of capital goods
15.Which of the following statements is not true for an infrastructure project?
(a) It has long gestation period
*(b) It reduces the risk for the lender as his funds get assure deployment for a long time.
(c) The debt equity ratio is normally high for an infrastructure project.
(d) The implementation period is usually long
16.Which of the following is not a source of funds for meeting the cost of purchase of fixed assets by an enterprise?
(a) Credit by supplier of assets (b) Internal accruals (c) Debentures *(d) DPG
17.Which of the following is a ratio indicative of the repayment capacity of a borrower?
(a) Quick ratio (b) TOLJTNW *(c) DSCR (d) DER
18.Which of the following is not correct regarding term loans by the banks?
(a) Asset liability matching is an important consideration in term financing
(b) Instalment•of term loan, payable within one year is considered as current liablility

(c) Repayment of a term loan can be in equated monthly instalments. *(d) Current ratio is the most important ratio in appraisal of a term loan 19. Project loans can be given by the bank to
(a) Only corporate (b) Only corporate and partnership firms
(c) Only corporate, partnership firms and societies *(d) Any business entity
20.Which of the following is not correct regarding infrastructure project by the banks?
(a) Banks are allowed to funds promoters' equity in certain circumstances
(b) Exposure norms are relaxed by RBI
*(c) Asset liability mismatch has been permitted by RBI
(d) MFG provides liquidity support to banks
21. Which of the following statements is not correct for project appraisal?
(a) Examination of technical feasibility is carried out
(b) The contribution of promoters forms a part of economic appraisal
(c) Promoters' background is part of the management appraisal
*(d) Capacity of promoters to arrange for additional funds, in case of contingencies, forms a part of economic appraisal
22.Which of the following is not a purpose of credit monitoring
(a) To ensure end use of the funds by the borrower
(b) To detect any deterioration in the security charged to the bank
(c) *To comply with the guidelines of the RBI
(d) To ascertain that the business continues to run on the projected lines
23.Which of the following is not a tool available to the bank for credit monitoring?
(a) *Sending regular reminders to the borrower
(b) Periodic visits to the business place for inspection
(c) Analysis of financial statements

(d) Examine conduct of borrower's account

24.Which of the following is not a method of detecting wrong mention of inventory in a stock statement?

(a) Stock audit

(b) Inspection of stocks

(c) *Analysis of financial statements

(d) Cross-check from the balance sheet figure

25.Which of the following is not a method of detecting wrong mention of receivables in statement submitted by the borrower?

(a) *Analysis of financial statements

(b) Cross check from the balance sheet figure

(c) Receivables audit

(d) Inspection of books of account

26.Which of the following is not a danger sign about the direction of business of the borrower?

(a) Devolvement of LCs, invocation of Bank Guarantees

(b) Demand for higher limit

(c) Delays in submission of stock/receivables statements

(d) *Return of cheques/bills

27.Which of the following is not an unsatisfactory sign in conduct of the account of the borrower?

(a) Delay in payment of interest/instalments,

(b) Routing of transacrions with some other bank

(c) Frequent over drawings

(d) *High turnover

28.Which of the following is not the purpose of credit audit?

(a) Improvement in the quality of credit portfolio

(b) Review sanction process and compliance status of large loans

(c) Feedback on regulatory compliance

(d) *Stock inspection

29. Purpose of appointing bank's nominee on company's board of borrowing company is:

(a) *To keep a tab on the important decisions of the board

(b) To be a part of the management

(c) To guide the company for better working

(d) To safeguard the securities charged to the bank 30.Which of the following is not a risk mentioned in the Basel II Accord

(a) Operational risk (b) Market risk *(C) Default risk (d) Credit risk

31.Which of the following is not a credit risk?

(a) Unwillingness of a customer to meet his commitment relating to a financial transaction with the bank.

(b) Inability of the customer to reimburse the bank in case of invocation of a guarantee or devolvement of an L.C.

(c) Inability of a customer to meet his commitment relating to a financial transaction with the bank.

(d) *Loss to the bank due to fraud.

32.Which of the following is an external factor affecting credit risk

(a) *Government policies

(b) Faulty loan and repayment structuring

(c) Overexposure (concentration) of credit to a particular segment

(d) Lack of an efficient recovery machinery

33.Which of the following is not an internal factor affecting credit risk

(a) Excessive lending to cyclical industries

(b) Low quality of credit appraisal and monitoring

(c) Deficiencies in the loan policy of the bank

(d) *Protectionist policies of other countries.

34.Which of the following is not a macro level action for mitigation of credit risk/

(a) Periodically reviews of the exposure norms for single and group borrowers

(b) *Improving appraisal standards of credit proposals
(c) Frequent reviews of norms and fixing internal limits for aggregate commitments to specific sectors of the industry/business
(d) Periodic review of total credit portfolio based on quality parameters
35.Which of the following is not a micro level action for mitigation of credit risk?
(a) Improving sanctioning and delivering process
(b) Obtention of collateral security
(c) Monitoring and review of individual proposals/categories of proposals
(d) *Periodical reviews of the exposure limits for business/industry segment
36.Which of the following statements is not true regarding credit derivative products?
(a) These are used to hedge credit risk to the bank
(b) The protection buyer is the lending bank
(c) The protection seller can be another bank or any other organization
(d) *The credit asset is transferred in case of derivatives
37.Credit rating is a system of
(a) *Measuring risk
(b) Mitigating risk
(c) Migrating risk
(d) Credit appraisal
38.Internal rating means:
(a) Rating the project
(b) Rating the promoters
(c) Rating the risk for internal use.
(d) *None of the above
.39.For external credit rating, banks depend on
(a) *Rating agencies
(b) Experienced staff of the bank
(c) Banking consultants
(d) None of the above
40.Which of the following is not an approach for assessment of credit risks, laid down under Basel II Accord?
(a) Standardised approach
(b) Foundation Internal Rating Based (IRBO approach
(c) Advanced Internal Rating Based (IRB) approach
(d) *Simplified Internal Rating Based (IRB) approach
41.Which of the following statements is true regarding Standardised approach?
(a) *It has already been adopted by all the banks
(b) It has been adopted only foreign banks operating in India.
(c) It has been adopted by the foreign banks operating in India and some of the Indian banks
(d) It has to be adopted by the all the banks by March 2010
42.RB1 has suggested which of the following earliest date of making application by banks to RBI regarding implementation of the advanced approaches (Foundation as well as Advanced IRB)?
(a) *1, April 2012
(b) 1, April 2013
(c) 1, April 2014
(d) 1, April 2015
43.The aim of a rehabilitation programme is:
(a) *To make the operations of the enterprise viable again
(b) To help in employment generation
(c) To comply with RBI guidelines
(d) To increase bank's-advances
44. Banks enter into compromise with borrowers in case of default, because:
(a) Recovery through legal action is time consuming
(b) Adequate security is not available
(c) Realisation or security may be difficult3 (d)- *All the above **(ANSWER IS - * MARKS)**

TEST YOUR SELF: PRIORITY SECTOR ADVANCES

01 RBI has revised the priority sector lending guidelines with effect from April 23, 2015 on the basis of recommendations of an Internal Working Group (IWG) headed by:
a) Ms Lily Vadera b) M. V. Nair c) C S Murthy d) R. Gandhi

02 Which of the following has/have been included as part of priority sector?
a) Medium enterprises b) Social Infrastructure c) Renewable Energy, d) None of these, e) All of these

03 Which of these has been added in the list of priority sector?
a) Agriculture b) Small Enterprises c) Medium Enterprises d) Educational Loan

04 As per April 15 guidelines on Priority Sector, which of the following distinctions have been dispensed with?

a) Micro and Small Enterprises
b) Marginal and Small farmers
c) Direct and indirect agricultural advances
d) Self Help Group and Joint Liability Group

05 Within agriculture, the target for lending to small and marginal farmers has been prescribed as ___% of ANBC or CEOBE whichever is higher. a) 5% b) 6% c) 7.5% d) 8%

06 The target for lending to Micro enterprises has been prescribed as ___% of ANBC or CEOBE whichever is higher. a) 5% b) 6% c) 7.5% d) 8%

07 As per April 15 guidelines on Priority Sector, the target for lending to weaker sections has been increased to of ANBC or CEOBE, whichever is higher.
a) 8% b) 10% c) 12% ,d) There is no change in the target for weaker sections.

08 Foreign Banks with 20 branches and above in India are required to achieve priority sector targets and sub-targets for Agriculture and Weaker Sections by ___.
a) March 31, 2018 b) 2019-20 c) 2020-21 d) 2015-16

09 Foreign Banks with less than 20 branches in India are required to achieve priority sector targets and sub-targets for Agriculture and Weaker Sections by ___.
a) 2018-19 b) 2019-20 c) 2020-21 d) 2015-16

10 Bank loans to food and agro processing units will form part of _____.
a) Agriculture b) Small Enterprises c) Indirect agriculture d) Medium enterprises

11 Export credit upto ____% of ANBC or CEOBE, whichever is higher, will be eligible as part of priority sector for foreign banks with less than 20 branches. a) 10% b) 25% c) 32% d) 40%

12 For domestic commercial banks and foreign banks with 20 or more branches in India, the incremental export credit over corresponding date of the preceding year will be reckoned as priority sector upto ____% of ANBC or CEOBE, whichever is higher. a) 1% b) 2% c) 5% d) 10%

13 The priority sector non-achievement will be assessed on _____ average basis at the end of the respective year from 2016-17 onwards.
fortnightly b) monthly c) quarterly d) half yearly e) yearly

14.As per revised guidelines on PS (April 15), for domestic commercial banks, the target for Priority sector will be _____of Adjusted Net Bank Credit (ANBC) or Credit Equivalent Amount of Off-Balance Sheet Exposure (CEOBE), whichever is higher.
a)32% b) 40% c) 42% d) 25%

15. Within the 18% target for agriculture, target for Small and Marginal Farmers will be 8% of ANBC or CEOBE, whichever is higher. This target to be achieved in a phased manner i.e., 7% by _____and 8% by
a)March 2017, March 2018 ; b) March 2018, March 2019 c)March 2016, March 2017 ; d)March 2015, March 2016

16.The target for Micro Enterprises i.e. 7.5% of ANBC or CEOBE, whichever is higher to be achieved in a phased manner i.e. 7% by _____and 7.5% by _____ a)March 2017, March 2018 ; b) March 2018, March 2019 c)March 2016, March 2017 ; d)March 2015, March 2016

17. For computation of Adjusted Net Bank Credit, following components are considered – (1) Bank Credit in India; (2) Bills Rediscounted with RBI and other approved Financial Institutions; (3) Bonds/debentures in Non-SLR categories under HTM category+ other investments eligible to be treated as priority sector +Outstanding Deposits under RIDF and other eligible funds with NABARD, NHB and SIDBI on account of priority sector shortfall + outstanding PSLCs; (4) Eligible amount for exemptions on issuance of long-term bonds for infrastructure and affordable housing; (5) Eligible advances extended in India against the incremental FCNR (B)/NRE deposits, qualifying for exemption from CRR/SLR requirements. Which of the following is correct regarding calculation of ANBC? : a) 1–2+3-4-5 b) 1+2+3-4-5 ; c) 1-2+3+4-5 d) 1-2-3+4+5

18. Lending to agriculture sector has been re-defined to include which of the following? : a) Farm Credit ; b) Agriculture Infrastructure , c) Ancillary activities d) Both (a) and (b) only & e) All of these

19. Which of the following is not part of agricultural advance?
a) Crop loans to farmers, which will include traditional/non-traditional plantations and horticulture, and, loans for allied activities.
b) Housing Loan to farmers for their own residence. ;
c) Medium and long-term loans to farmers for agriculture and allied activities
d) Loans to farmers for pre and post-harvest activities, viz., spraying, weeding, harvesting, sorting, grading and transporting of their own farm produce

20.As per revised guidelines on PS (April 15), loans to farmers up to _____ against pledge/hypothecation of agricultural produce (including warehouse receipts) for a period not exceeding 12 months ; a) Rs 10 lakh b) Rs 20 lakh; c) Rs 50 lakh d) Rs 100 lakh

21 Which of the following is not an agricultural advance?
a) Loans to distressed farmers indebted to non-institutional lenders.
b) Loans to farmers under the Kisan Credit Card Scheme.
c) Loans to all farmers for purchase of land for agricultural purposes.
d) None of these

22 Loans to corporate farmers, farmers' producer organizations/companies of individual farmers, partnership firms and co-operatives of farmers directly engaged in Agriculture and Allied Activities, viz., dairy, fishery, animal husbandry, poultry, bee-keeping and sericulture will be part of priority sector provided loan is up to _____ per borrower. a) Rs 2 crore b) Rs 5 crore c) Rs 10 crore d) None of these

23 Loans for construction of storage facilities (warehouses, market yards, godowns and silos) including cold storage units/ cold storage chains designed to store agriculture produce/products, irrespective of their location will be part of priority sector provided aggregate sanctioned limit from the banking system is up to Rs _____ per borrower -a) Rs 10 crore b) Rs 20 crore c) Rs 50 crore d) 100 crore

24 Which of the following is not part of agriculture infrastructure as per PS guidelines issued in April 15?
a) Loans for construction of storage facilities to store agriculture produce/products.
b) Soil conservation and watershed development.
c) Plant tissue culture and agri-biotechnology, seed production, production of bio-pesticides, bio-fertilizer, and vermi composting. d) None of these

25 Loans to co-operative societies of farmers for disposing of the produce of members will be part of agriculture provided loan is up to Rs. a) Rs 1 crore b) Rs 2 crore c) Rs 5 crore d) Rs 10 crore

26 Loan for Food and Agro-processing will be part of Agricultural advance provided sanctioned limit from the banking system is up to _____ per borrower ;
a) Rs 10 crore b) Rs 20 crore c) Rs 50 crore d) Rs 100 crore

27 Which of the following is not part of agricultural advance?
a) Loans for setting up of Agriclinics and Agribusiness Centres.
b) Bank loans to Primary Agricultural Credit Societies (PACS), Farmers' Service Societies (FSS) and Large-sized Adivasi Multi-Purpose Societies (LAMPS) for on-lending to agriculture
c) Loans sanctioned by banks to MFIs for on-lending to agriculture sector.
d) Outstanding deposits under SEDF and other eligible funds with SIDBI on account of priority sector shortfall.

28 Farmers with landholding of up to _____ are considered as Marginal Farmers and farmers with a landholding upto ____ are considered as Small Farmers
a) 1 hectare, 2 hectares b) 2.5 hectare, 5 hectare c) 1 hectare, 2.5 hectare,d) 5 hectare, 10 hectare
29 Loans to farmers' producer companies of individual farmers, and co-operatives of farmers directly engaged in Agriculture and Allied Activities, is classified as Small and Marginal farmer where the membership of Small and Marginal Farmers is not less than ____ by number and whose land-holding share is also not less than ____of the total land-holding
a) 50%; 50% b) 50%; 75% c) 75%; 75% d) 75%; 50%

30 Which of the following will not be classified as priority sector advance?
a) Loan to Micro manufacturing enterprises
b) Loan to Small manufacturing enterprises
c) Loan to Medium manufacturing enterprises, d) None of these

31 Bank loan to Micro, Small and Medium manufacturing Enterprises will be part of priority sector provided the loan is up to _____. a) Rs 5 crore,b) Rs 10 crore c) Rs 20 crore d) Irrespective of amount of loan

32 Bank loan to Micro and Small service Enterprises will be part of priority sector provided the loan is up to _____. a) Rs 2 crore b) Rs 5 crore c) Rs 10 crore d) Rs 20 crore e) None of these

33 Bank loan to Medium service Enterprises will be part of priority sector provided the loan is up to _____.
a) Rs 2 crore b) Rs 5 crore c) Rs 10 crore d) Rs 20 crore e) None of these

34 Loans to units in the Khadi and Village Industries sector will be eligible for classification as Micro enterprise under the sub-target of 7%/7.5% prescribed for Micro Enterprises under priority sector provided the investment in plant and machinery is up to _____.
a) Rs 10 lakh b) Rs 25 lakh c) Rs 2 crore d) Rs 5 crore e) None of these

35 Credit outstanding under General Credit Cards (including Artisan Credit Card, Laghu Udyami Card, Swarojgar Credit Card, and Weaver's Card etc. catering to the non-farm entrepreneurial credit needs of individuals) will be part of advance to Micro and Small enterprises provided the loan is up to _____.
a) Rs 50,000 b) Rs 500,000 c) Rs 10,00,000 d) None of these

36 Which of the following is not part of Micro, Small and Medium enterprises under priority sector advance?
a) Loans to entities involved in assisting the decentralized sector in the supply of inputs to and marketing of outputs of artisans, village and cottage industries.
b) Loans to co-operatives of producers in the decentralized sector viz. artisans, village and cottage industries.
c) Loans sanctioned by banks to MFIs for on-lending to MSME sector.
d) Outstanding deposits with SIDBI on account of priority sector shortfall.
e) None of these

37 As per revised PS guidelines (April 15) banks are required to lend 40% of advance to Micro and Small enterprises to units with investment in plant and machinery up to_____.
a) Rs 2 lakh b) Rs 4 lakh c) Rs 10 lakh d) None of these as there is no such target.
38 The MSME units will continue to enjoy the priority sector lending status up to _____years after they grow out of the MSME category concerned.
a) one b) two c) three d) four e) None of these

39 Incremental export credit over corresponding date of the preceding year, up to 2% of ANBC or CEOBE, whichever is higher, effective from April 1, 2015 will be part of priority sector provided sanctioned limit is up to ___per borrower and annual turnover of up to _____.
a) Rs 5 crore; Rs 10 crore b)Rs 10 crore; Rs 25 crore c) Rs 25 crore; 100 crore d) Rs 50 crore; Rs 100 Cr.

40 Loans to individuals for educational purposes including vocational courses in India will be part of Priority sector provided loan is up to _____. a) Rs 5 lakh b) Rs 10 lakh c) Rs 20 lakh d) Rs 25 lakh

40 Loans to individuals for educational purposes for studies abroad will be part of Priority sector provided loan is up to _____. a) Rs 5 lakh b) Rs 10 lakh c) Rs 20 lakh Rs 25 lakh e) None of these

41 A loan of Rs 20 lakh has been sanctioned to an individual for studies in India. How much of it will be part of priority sector? a) Rs 5 lakh b) Rs 10 lakh c) Rs 20 lakh d) None of these

42 Loan for purchase/construction of a dwelling unit per family in a metropolitan area will be classified as priority sector provided loan is up to _____ and the overall cost of the dwelling unit does not exceed ____.
a) Rs 28 lakh; Rs 35 lakh,b) Rs 24 lakh; Rs 30 lakh c) Rs 20 lakh; Rs 25 lakh d) Rs 32 lakh; Rs 40 lakh

43 Loan for purchase/construction of a dwelling unit per family in a place with population less than 10 lakh will be classified as priority sector provided loan is up to _____ and the overall cost of the dwelling unit does not exceed ____.
a) Rs 28 lakh; Rs 35 lakh, b) Rs 24 lakh; Rs 30 lakh, c) Rs 20 lakh; Rs 25 lakh, d) Rs 32 lakh; Rs 40 lakh

44 Loans for repairs to damaged dwelling units will be part of priority sector provided loan is up to ____in metropolitan centres and up to _____ in other centres.
a) Rs 2 lakh, Rs 1 lakh b) Rs 5 lakh, Rs 2 lakh ,c) Rs 4 lakh; Rs 2 lakh d) Rs 10 lakh; Rs 5 lakh

45 Bank loans to any governmental agency for construction of dwelling units or for slum clearance and rehabilitation of slum dwellers will be part of priority sector provide loan is up to _____ per dwelling unit.
a) Rs 2 lakh b) Rs 5 lakh c) Rs 10 lakh ,d) Rs 20 lakh e) None of these

46 Loans for housing projects exclusively for the purpose of construction of houses for economically weaker sections and low income groups, will be part of priority sector provide the total cost of the house does not exceed _____ per dwelling unit a) Rs 1 lakh b) Rs 2 lakh c) Rs 5 lakh d) Rs 10 lakh

47 Loans for housing projects exclusively for the purpose of construction of houses for economically weaker sections and low income groups, the total cost of which does not exceed Rs 10 lakh per dwelling unit for the purpose of identifying the economically weaker sections and low income groups, the annual family income should not be more than_____.

a) Rs 50,000 in rural areas and Rs 100,000 in other areas
b) Rs 100,000 in rural area and Rs 200,000 in other areas
c) Rs 160,000 irrespective of location d) Rs 200,000 irrespective of location

48 Bank loans to Housing Finance Companies (HFCs), approved by NHB for their refinance, for on-lending for the purpose of purchase/construction/reconstruction of individual dwelling units or for slum clearance and rehabilitation of slum dwellers, will be part of priority sector provided aggregate loan limit is up to _____ per borrower. a) Rs 10 lakhb) Rs 5 lakh , c) Rs 2 lakh d) Rs 20 lakh

49 Bank loans for building social infrastructure for activities namely schools, health care facilities, drinking water facilities and sanitation facilities in Tier II to Tier VI centres will be part of priority sector provided loan is up to ____per borrower.
a) Rs 5 crore b) Rs 1 crore , c) Rs 2 crore d) Rs 10 crore

50 Bank loans to borrowers for purposes like solar based power generators, biomass based power generators, wind mills, micro-hydel plants and for non-conventional energy based public utilities viz. street lighting systems, and remote village electrification will be part of priority sector provided loan amount is up to_____.
a) Rs 5 crore b) Rs 10 crore c) Rs 15 crore d) Rs 20 crore e) Rs 25 crore

51 Bank loans to individual households for purposes like solar based power generators, biomass based power generators, will be part of priority sector provide the loan is up to _____ per borrower.
a) Rs 10 lakh b) Rs 20 lakh , c) Rs 25 lakh d) Rs 30 lakh

52 Loans to distressed persons other than farmers to prepay their debt to non-institutional lenders will be treated as other priority sector provided loan per borrower is limited up to _____
a) Rs 25000 b) Rs 50,000 c) Rs 100,000 d) Rs 200,000

53 Overdrafts upto Rs 5,000/- under Pradhan Mantri JanDhanYojana (PMJDY) accounts will be classified as other priority sector provided the borrowers household annual income does not exceed ____for rural areas and for non-rural areas.
a) Rs 60,000; Rs 120,000b) Rs 80,000; Rs 160,000 ,
c) Rs 100,000; Rs 1,60,000 d) Rs 100,000; Rs 200,000

54 Artisans, village and cottage industries are classified as weaker section provided individual credit limits do not exceed _____.
a. Rs. 50,000 ; b. Rs. 1.00 lac ; c. Rs. 2.00 lacs & d. Rs.5.00 lacs

ANSWER

1	A	11	C	21	C	31	D	41	B	51	A
2	E	12	B	22	A	32	B	42	A	52	C
3	C	13	C	23	D	33	C	43	C	53	C
4	C	14	B	24	D	34	E	44	B	54	B
5	D	15	C	25	C	35	D	45	C	55	
6	C	16	C	26	D	36	E	46	D	56	
7	D	17	A	27	D	37	D	47	D	57	
8	A	18	E	28	A	38	C	48	A	58	
9	B	19	C	29	C	39	C	49	A	59	
10	A	20	C	30	D	40	B	50	C	60	

FINANCIAL STATEMENT ANALYSIS

1. Balance Sheet is a statement of Assets and Liabilities or statement of Sources and Uses
*(a) as on a date (b) as on 31st March (c) for 12 months (d) for a particular period (e) none of these
2. Assets can be represented as :
(a) uses of funds (b) sources of funds (c)what the business owns *(d) both (a) and (c) above
3. Liabilities can be represented as :
(a) sources of funds (b) uses of funds (c) what the business owes *(d) both (a) and (c) above
4. Current assets are defined as :
(a) assets which are expected to be consumed within one year
(b) assets which are expected to be converted into cash within one year
*(c) either (a) or (b) (d) assets which are to paid out of current liabilities(e) none of the above
5. Fixed assets are defined as :
(a) assets which are fixed to the land *(b)assets which are acquired for production and not meant for sale
(c) assets which have a fixed value (d) assets which can not be sold easily (e) none of the above
6. Term liabilities are one :
(a) which are to be met within one year from the date of balance sheet
*(b) which are not payable within one year from the date of balance sheet
(c) which were raised for more than one year (d) which are not payable immediately (e) none of these
7. Current Liabilities are those liabilities
(a) which are payable within one year (b) which are expected to be met from proceeds of current assets
(c) which are payable after one year *(d) both (a) & (b) (e) both (b) & (c)
8. Which of the following is not classified as current asset?
(a) stocks (b) prepaid expenses *(c) pre operative expenses (d) book debts (e) none
Which of the following is classified as intangible or fictitious asset?
(a) Goodwill (b) Preliminary expenses (c) Accumulated losses (d) Deferred Revenue Expenses *(e) All of these
10. Which of the following is a current liability for calculation of current ratio?
(a) Sundry creditors (b) Borrowings from banks (c) Provision for tax
(d) Instalment of term loan payable within one year *(e) **All** of these
11. Debtors which are old for more than 6 months are to be classified as
(a) Current Assets (b) Intangible Assets (c) Non Current Assets (d) Fixed Assets
12. Instalments of term loan falling due within a year are treated as_ for calculation of current ratio :
*(a) current liability (b) current asset (c) term liability (d) net worth
13. Quick assets mean:
(a) **all** assets minus inventory (b) all current assets minus inventory
(c) assets other than cash (d) all current assets minus inventory and prepaid expenses
14. Sales minus cost of sales is referred to as :
(a) operating profit (b) net profit (c) profit before tax (d) profit after tax *(e) gross profit
15. Operating profit is arrived at by :
*(a) reducing administrative, general and selling expenses from gross profit

(b) adding back depreciation to gross profit (c) adding back depreciation and interest to net profit
(d) adding back interest expenses to gross profit (e) none of the above
16. Cash profit is:
(a) gross profit before depreciation (b) net profit after depreciation
(c) net profit before depreciation (d) gross profit after depreciation (e) none of these
17. Cash loss is:
(a) gross loss before depreciation (b) net loss after depreciation (c) net loss before depreciation
(d) gross loss after depreciation (e) none of these
18. Tangible net worth means :
*(a) Paid up capital and reserves minus intangible assets (b) Net worth minus investment in fixed assets
(c) Paid up capital and reserves minus instalment of term loan payable within one year
(d) Net worth minus current liabilities (e) Total Assets minus intangible assets
19. The term Liquid Surplus or Net working capital refers to :
(a) total investment in current assets (b) excess of current liabilities over current assets
*(c) excess of current assets over current liabilities
(d) excess of capital plus free reserves over term liabilities (e) none of the above
20. Net working capital will be positive when :
(a) current assets are more than current liabilities (b) current liabilities are more than current assets
(c) current ratio is more than one (d) when current ratio is less than one *(e) both (a) & (c)
21. Liquidity ratios include :
(a) Current Ratio (b) Quick Ratio (c) Debt equity ratio *(d) Both (a) & (b) (e) all above
22. Current Ratio is obtained by :
(a) reducing current liabilities from current assets and dividing the resultant figures by current liabilities
(b) dividing current liabilities by current assets *(c) dividing current assets by current liabilities
(d) dividing outside liabilities by net worth (e) none of the above
23. Current Ratio is an indicator of _____ of the borrower:
*(a) liquidity position (b) solvency (c) profitability (d) all above (e) none of the above
24. Current Ratio of less than 1 indicates that the borrower:
(a) has sufficient current assets to meet current liabilities (b) may be unable to pay current dues
(c) has borrowed excessively from outsiders (d) any of the above (e) none of the above
25. Current ratio as per second method of lending given by Tandon Committee works out to :
(a) 1:1- (b) 2:1 (c) 1.17:1 (d) 1.33 : 1 (e)none of these
26. Acid Test Ratio is supportive ratio for _____
(a) Debt-Equity Ratio (b) Current Ratio (c) Gross Profit Ratio
(d) Net Profit Ratio (e) Debt-Service Coverage Ratio
27. The following are the Current and Quick Ratio of a firm for two consecutive years
Current Ratio 1.6:1 & 2.3:1; Quick Ratio 1.1:1 & 1:1. The trend indicates that :
(a) the borrower is relying heavily on term loans
(b) there is reasonable investment from current liabilities in current assets
(c) there is excessive investment in inventory and prepaid expenses
(d) more sales are being effected on credit than before (e) none of the above
28. Debt Equity Ratio is relationship between :
(a) total liability and net worth (b) current assets and current liabilities
(c) term liabilities to total net worth *(d) term liabilities to tangible net worth (e) either (a) or (d)
29. A decreasing Debt Equity Ratio means :
*(a) higher stake of owners (b) lower stake of owners (c) decrease in profitability of the business
(d) sharp increase in profitability of the concern . (e) none of the above
30. Profit & Loss account helps in computing
(a) Profitability Ratio (b) Solvency Ratio (c) Turnover Ratio (d) Liquidity Ratio
31. Return on Investment (ROI) falls in the category of :
*(a) Profitability Ratios (b) Solvency Ratios (c) Liquidity Ratios (d) all above
32. Gross Profit Ratio is obtained by :
(a) dividing gross profits by net sales and multiplying it with 100

(b) dividing net profit by gross sales and multiplying it with 100
(c) dividing gross profit by gross sales and multiplying it with 100
(d) net sales by net profit (e) none of the above
33. Which of the following ratios is one of the most important ratios to ascertain the profitability ?
(a) Debt Equity Ratio (b) Return on Investment (c) Working Capital Turnover Ratio
(d)Gross Profit Ratio (e) Quick Ratio
34. 'Activity Ratios' or 'Turnover Ratios' indicate :
(a) extent of profitability *(b) efficiency of the concern in the utilisation of assets
(c) stake of owners' funds (d) stake of term lending institutions (e) none of the above
35. Debtors Velocity Ratio indicates :
(a) proportion of credit sales to annual sales (b) proportion of credit sales to fixed assets
(c) average time-lag between sales and the collection of debts
(d) average time taken in effecting sales to customers (e) none of the above
36. A decreasing trend of Debtors Velocity Ratio implies :
(a) more credit being extended (b) less likelihood of bad and doubtful debts (c) poor debt collection
(d) more demand for product of the seller (e) none of the above
37. Debt Service Coverage Ratio (DSCR) indicates :
*(a) capability of unit to generate adequate cash accruals to pay instalments of term loans and interest thereon (b) knowing short term liquidity of borrower (c) overall profitability of the unit
(d) ascertaining borrower's stake in business (e) none of the above
38. Debt Service Coverage Ratio is used for sanction of :
(a) Working Capital Facilities *(b) Term Loans (c) Bank Guarantee (d) Letter of Credit
39. Ideal DSCR is
a) 1:1 (b) 1.33:1 (c) 1.5:1 *(d) 2:1 (e) None of these
40. Short term solvency of a unit is indicted by
a) Debt equity Ratio b) Total indebtedness ratio c) proprietary ratio *d) Current ratio
41. A very high Current Ratio of say 4:1 is :
(a) highly desirable as it shows capacity of the borrower to repay current dues without difficulty
*(b) not desirable as it means less efficient use of funds
(c) desirable as it means that the borrower is relying more on capital and reserves than on outside borrowings (d) desirable as it ensures safety of bank funds in the long run (e)none of the above
42. Proprietory Ratio is the relationship between :
(a) total assets to tangible net worth *(b) capital or shareholders' funds to total tangible assets
(c) net fixed assets to long-term debts (d).either (a) or (b) (e) none of the above
43. For calculating Debt Service Coverage Ratio (DSCR), the numerator will be :
*(a) Profit after tax plus depreciation plus interest on term borrowings
(b) Profit before tax plus depreciation plus interest on term borrowings
(c) Profit after tax plus interest on term borrowings (d) Profit before tax plus interest on term'borrowings
44. Which of the following is incorrect?
(a) For a dealer of cars, a car is a current asset
(b) Security deposits for electricity or telephone is a non current asset.
(c) Prepaid rent is a current asset
*(d) For a transport operator, a car is a current asset (e)Pre expenses is a fictitious asset
45. The short term solvency of a unit can be judged by
a) Debt Equity Ratio *b) Current Ratio c) Debt collection period
d) Gross profit margin e) None of these
46. Debt Equity Ratio is calculated by dividing
*(a) Long term liability by tangible net worth b) Long term liability by paid up capital and reserves
(c) Tangible net worth by long term liability d) Paid up capital and reserves by long term liability
(e) Total outside liability by paid up capital
47. Working capital gap means
(a) Current Assets minus Current Liability
*(b) Current Asset minus Current Liability other than bank borrowing (c)

Current Assets minus inventory & prepaid expenses
(d) Current Assets minus paid up Stocks
(e) Quick Assets minus Current Liability other than bank borrowing
48. Which of the_following is not a fixed cost of a manufacturing unit? a) raw material consumed b) rent paid for factory shed c) consumption of power
d) salary of the office staff e) commission paid to salesmanf) salary of manager
g) wages paid to production staff based on production *(h) a,c,g & e (1) none
49. Break even point in a production process is the point where:
a) fixed costs equal variable costs (b) fixed costs start rising on further production
*(c) total of fixed and variable costs just equals the total revenue (d) both (a) and (c)
50. Break Even Point represent a level of sales at which :
(a) there is no profit or loss (b) sales revenue is equal to total cost
(c) a firm is able to recover both fixed and variable costs *(d) all of these (e) none of these
51. Operating cycle in an industrial concern means
a) Conversion of raw materials into semi-finished goods
b) *Conversion of raw materials into finished goods sundry debtors and back into cash
c) Conversion of raw materials into finished goods
d) Conversion of sundry debtors into cash e) none
52. As per first method of lending of Tendon Committee bank should finance 75% of:
*a) working capital gap (b) total current assets (c) net working capital
d) lower of (a) or (b) above (e) none
53. In the second method of lending under Tendon Committee:
(a) Bank should finance 75% of working capital gap
(b) Bank should finance 50% of the current assets
*(c) Borrower should contribute 25% of total current assets and total current liabilities including bank borrowing should not exceed 75% of current assets
(d) Lower of (a) & (b) e) none
54. As per Nayak Committee recommendations as modified from time to time, 20% of projected sales are to be sanctioned as working capital to SSI units with WC limits up to
a) Rs. 50 lakh b) Rs. 100 lakh c) Rs. 200 lakh *d) Rs. 500 lakh e) none
55. Funds flow statement means:
(a) operating statement for a period (b) statement of sources and use of funds as on a date
*(c) statement of sources and use of funds for a period (d) statement of assets and liabilities as on a date
56. Which of the following is a long term source?
a) Paid up capital and reserves b) Term loan from financial institution
c) Plant and machinery *d) Both (a) & (b) e) Both (b) & (c)
57. Which of the following is not a long term use?
a) Goodwill b) Land & Building c) Investment in subsidiaries
*d) Debentures e) Pre operative expense
58. The profit retained in the business are classified as
b) Current asset as these are easily realizable (b)Current liability as these are payable to shareholders
c) Assets as these are owned by business *(d) Liabilities as this represent as a source of funds
e) Long term liability as these are payable to shareholders after one year
59. Which of the following is incorrect?
c) Increase in liabilities is a source of funds b) Decline in assets is a source of funds
c) Increase in assets is a use of funds d) Decline in liabilities is a use of funds *e) None of these

NON PERFORMING ASSETS

1. What is the objective of introducing prudential norms for income recognition, asset classification and Provisioning for the advances portfolio of the banks by RBI?
(a) for greater consistency in the published accounts (b) for transparency in the published accounts
(c) to apply principle of conservatism *(d) Both (a) & (b) (e) All of these
2. Non Performing Assets (N PAs) are categorized as:
(a) Sub Standard Assets **(b)** Doubtful Assets (c) Loss Assets *(d) any one of the above

3. With effect from the year ending 31.03.2004, a term loan is treated as non-performing asset (NPA) if : (a) the balance outstanding is more than the loan amount originally sanctioned
(6) interest remains overdue for more than 90 days
(c) installment remains overdue for more than 90 days
*(d) interest and/or installment remain overdue for more than 90 days (e) both (a) and (d) above
4. As from the year ending 31.03.2004, a cash credit/overdraft account is classified as NPA if :
(a) balance.is beyond the sanctioned limit / D.P (b) interest has not been serviced for 4 quarters
*(c) the account remains out of order (d) both (b) and (c) (e) none of these
5. Crop loan granted for long duration crop becomes NPA if :
(a) interest remains unpaid after it has become overdue for two years
(b) interest and /or installment remains unpaid after it has become overdue for two crop seasons
(c) interest and/or installment of principal remains unpaid after **it** has become overdue for two half years
(d) interest and/or installment of principal remains unpaid after it has become overdue for two crop seasons but for a period not exceeding two half years
*(e) interest or instalment is overdue for one crop season.
6. Crop loan granted for short duration crop will become NPA if:
(a) the loan is overdue for 6 months (b) the loan is overdue for 12 months
*(c) the loan is overdue for two crop season (d) the loan is overdue for more than 2 crop seasons
7. Out of order account means an account where:
(a) the balance is continuously more than the sanctioned limit or drawing power
(b) where as on the date of Balance Sheet, there is no credit in the account continuously for 90 days or credit is less than interest debited
(c) where stock statement has not been received for 3 months or more.
*(d) any of these (e) only (a) or (b)
8. In case of cash credit and overdraft, the account will be treated as NPA if
(a) the limit is not renewed/reviewed within 6 months from the due date of renewal.
(b) account remains out of order.
(c) the limit is not renewed within 3 months from the due date of renewal
*(d) Either (a) or (b) (e) none of these
9. Which of the following accounts will be classified as NPA?
(a) Loan against LIP when the balance outstanding is more than the limit sanctioned for 6 months but within surrender value of LIP
(b) Interest debited in the educational loan account during moratorium period has not been recovered simultaneously.
(c) Interest debited in a housing loan account for last 6 mouths has not been recovered from the date of sanction and repayment was to start after 12 months from sanction.
(d) Loan is guaranteed by Central Govt and is overdue for more than 90 days.
*(e) None of these
10. Which of the following is not correct regarding income recognition in respect of NPA accounts?
(a) Banks should not charge and take to income account interest on any NPA.
(b) Interest on advances against term deposits, NSCs, IVPs, KVPs and Life policies may be taken **to** income account on the due date, provided adequate margin is available in the accounts.
(c) If Central Government guaranteed advances become NPA, the interest on such advances should not be taken to income account unless the interest has been realised. *(d) None of these
11. As per RBI guidelines, w.e.f the year ending 31.03.2005 when an asset is identified as NPA it **will** be classified as sub-standard up to a period not exceeding :
(a) 18 months (b) 5 years (c) 6 months *(d) 12 months (e) None of these
12. As per RBI guidelines, w.e.f the year ending 31.03.2005, an account will be classified as Doubtful if it is NPA or sub standard for more than:
(a) 6 months *(b) 12 months (c) 18 months (d) 24 months (e) None of these3 years
13. An NPA account is straightaway classified as doubtful without waiting for 12 months if the security deteriorates so much that its realizable value is:

(a) less than 10% of the outstanding balance (b) 10% or above the outstanding balance
*(c) 10% or above but less than 50% of the outstanding balance
(d) 10% or below the outstanding balance (e) None of these

. An NPA account is straightaway classified as loss . if the security deteriorates so much that its realizable value is:
*(a) less than 10% of the outstanding balance (b) 10% or above the outstanding balance
(c) 10% or above but less than 50% of the outstanding balance
(d) 10% or below the outstanding balance (e) None of these
15. In an NPA account, interest or any other charge will be recognized as income as per which of the following:
(a) on accrual basis (b) when borrower gives a firm commitment to regularize the account
*(c) when it is actually realised (d) (a) or (c) as per policy of the bank (e) None of these
16. A crop is considered as long duration crop if crop season is more than 12 months. The crop season for each crop which means the period up to harvesting of the crops raised, is determined by:
(a) Banks themselves *(b) State Level Banker's Committee (c) NABARD (d) RBI
17. Provisioning is required to be made in the case of___ assets.
a) Standard b) Sub standard c) Doubtful d) Only (b) & (c) *e) All of these
18. On which of the following types of loans, provision is required to be made at the rate of 0.25% of the outstanding if the advance is classified in the standard category?
*a) Direct advance to agriculture (b) Direct advance to SME
c)All advances to Agriculture & SME (d) Both (a) & (b) (e) None of these
19. The provision on standard assets made to a person other than Direct advance to agriculture and SME and
for commercial real estate are to be made at the rate of _____of the outstanding balance on global basis.
a) 0.25% *b) 0.40% c) 1% d) 0.50% e) None of these
20. Which of the following is correct regarding provision on standard assets in the following categories? *a) Commercial Real estate: 1% of outstanding balance
b) Housing loan more than 30 lakh: 1% of the outstanding balance
c) Capital market exposure: 2% of the outstanding balance d) Both (a) & (b) only(e)-None of these
21. In the case of advances classified as sub standard assets other than those which were unsecured abinitio, the provision is required to be made as per which of the following?
a) For unsecured portion 100% and on secured portion 10%.
b) For unsecured portion 100% and on secured portion 20%.
*c) 15% of the outstanding balance without reference to security d) None of these
22. In the case of sub standard assets which were unsecured abinitio, the provisioning is required to be made
at the rate of_____ of outstanding balance.
*a) 25% b) 50% c) 75% d) 100% e) None of these
23. A clean overdraft has become NPA and the outstanding is Rs 100,000. How much provision is to be made?
(a) Rsl 0,000 *(b) Rs 25,000 (c) Rs 50,000 (d) Rs 100,000 (e) None of these
24. An advance was granted to farmer for poultry. Account is standard and outstanding in the_account is Rs 100,000 whereas realizable value of security is Rs 60,000 only. How much provision is to be made?
(a) Rs 10,000 *(b) Rs 250 (c) Rs 40,150 (d) Rs 400 (e) None of these
25. An advance has been granted to a farmer for construction of house. The account is standard and outstanding in the account is Rs 100,000. How much provision is to be made on this account?
(a) Rs 250 *(b) Rs 400 (c) Rs 1000 (d) None of these
26. In the case of doubtful accounts, provision on unsecured portion is made at the rate of 100%. For secured portion, the provision is made as a percentage of realizable value of security depending upon the period for which the account is doubtful. For which of the following, the rate of provision for secured portion is not correct?
a) DF1: 25% b) DF2: 40% *c) DF3: 50% d) DF3: 100% e) None of these

27. A loan has become more than 3 years old in the doubtful category. In this case, the provision on secured portion as on 31.3.10 will be:
a) 50% b) 60% c) 75% *d) 100% e) None of these
28. An advance of Rs. 2,00,000 has been declared sub standard on 31.10.2011. It is covered by securities with realizable value of Rs. 1,50,000 . Total provision in the account as on 31.03.2012 will amount to:
*(a) Rs. 30000 (b) Rs. 30,200 (c) Rs. 47,000 (d) Rs. 83,800 (e) none
29. The unsecured exposure which are classified as sub standard attract a provision of 25% of the outstanding balance. For this purpose, unsecured exposure means an exposure where the realisable value of the
security, as assessed by the bank/approved valuers/Reserve Bank's inspecting officers, is _, *ab--initio,* of the outstanding exposure.
*(a) not more than 10% (b) not less than 10% (c) less than 10% (d) None of these
30. A cash credit account other than agriculture and commercial state became out of order on 5.3.12. Balance outstanding in the account is Rs 200,000. Value of security in the account is Rs 150,000. How much provision is required to be made as on 31.3.12?
(a) Rs 20,000 (b) Rs 50,000 (c) Rs 15,000 *(d) Rs 800
31. An account became sub standard on 5.3.09. Balance outstanding in the account is Rs 5 lac and realizable value of security is Rs 4 lac. How much provision is required to be made as on 31.3.12.
(a) Rs 50,000 (b) Rs 220,000 (c) Rs 100,000 *(d) Rs 500,000 (e) None of these
32. How is the provision on standard assets treated?

(a) it is deducted from Gross NPA (ii) it is deducted from Gross advances
*(c) shown as 'Contingent Provisions against Standard Assets' under 'Other Liabilities and Provisions -Others' in Schedule 5 of the balance sheet.
(d) any of these but accounting practice should be followed consistently. (e) None of these
33. An advance has been made by 3 banks under a consortium arrangement. The account becomes NPA with one of the banks, What should be done by other banks?
(a) classify the account as NPA (b) classify the account as NPA but provision not to be made
*(c) the account will be classified as per record of recovery of each bank
(d) classify the account as NPA if the same is NPA with the leader bank (e) None of these
34. Advance against which of the following will be subject to provisions of Asset classification, income Recognition and Provisioning even if sufficient margin is available?
(a) own deposit (b) NSC *(c) government securities (d) LIP (e) None of these
35. RBI has proposed that total provisioning coverage ratio of banks, including floating provisions, should not be less than _____ . Banks should achieve this norm not later than end-September 2010
(a) 30% (b) 40% (c) 50 *(d) 70% (e) None of these
%
36. Which of the following is true about treatment of floating provisions?
(a) Floating provisions can be deducted from gross NPAs to arrive at net NPAs
(b) Floating provisions can be treated as part of Tier II capital
'lc) Either (a) or (b) (d) Both (a) & (b) (e) None of these
37. Cases with claims of _ are filed with DRT and not with normal courts.
(a) less than Rs 10 lakh (b) Rs 10 lakh *(c) Rs 10 lakh and above (d) Rs 20 lakh
38. Choose incorrect statement(s) regarding appeal to the Appellate Tribunal against the order of the Debt Recovery Tribunal :
(a) When a Debt Recovery Tribunal has passed an order with the consent of the parties, no appeal lies with the Appellate Tribunal.
*(b) An appeal to the Apellate Tribunal is required to be preferred within 90 days from the date of receipt of order of the Debt Recovery Tribunal by the aggrieved party.
(c) When the aggrieved party is required to pay the amount to bank/financial institution, the Appellate Tribunal will entertain appeal only when 75% of the amount ordered to be paid by the Debt Recovery Tribunal is deposited by him which can be reduced to 0% by DRAT.

(d) all of these (e) only (b) and (c)
39. Appeal against the judgement of DRT can be made to DRAT within how many days?
(a) 30 days of judgement (b) 45 days of judgement *(c) 45 days of receiving copy of judgement
(d) 30 days of receiving copy of judgement. (e) None of these
40. Lok Adalats are set up under provisions of
(a) Debt Recovery Act 1993 *(b) Legal Services Authority Act 1987 (c) Indian Contract Act 1872
(d) General Clauses Act (e) None of these
41. Which type of accounts can be taken to Lok Adalat?
(a) Sub standard (b) Doubtful (c) Loss accounts *(d) Only (b) & (c) (e) All of these
42. Cases covered under Lok Adalats are both suit filed and non-suit filed accounts, which are in 'doubtful' and 'loss' categories with outstandings up to:
(a) Rs. 2 lacs (b) Rs. 5 lacs (c) Rs.10 lacs *(d) Rs. 20 lacs (e) Rs. 7.5 lacs
43. Banks prefer filing cases with Lok Adalats because:
*a) No court fees is payable (b) this is an informal arrangement
c) Bank can recover loss assets d) Only (a) & (b) e) None of these
44. Which of the following is not correct regarding Lok Adalat?
(a) Since its decisions are consent decree, no appeal can be filed against decision of Lok Adalat.
(b) If Lok Adalat is arranged by DRT, .cases involving amount of more than Rs 20 lakh can also be filed
(c) Filing a case with Lok Adalat does not extend limitation period.
(d) Its awards are deemed to be decrees of civil courts. *(e) None of these
45. To enforce its rights under SARFAESI Act,2002, a bank is required to give days notice to borrower.
(a) 30 (b) 45. (c) 90 *(d) 60 (e) 120
46. To enforce its rights under SARFAESI Act,2002, minimum outstanding in the account should be:
(a) Rs 1 lac *(b) more than Rs 1 lac (c) Rs 10 lakh (d) More than Rs 10 lakh
47. Provisions of Sarfaesi Act are not applicable in the case of:
(a) securities under lien or pledge (b) agricultural land *(c) Both (a) & (b) (d) None
48. Provisions of Sarfaesi Act are not applicable and securities can not be acquired if % of the principal amount has been paid.
(a) 50% (b) 60% (c) 75% *(d) 80% (e) None of these
49. In the case of consortium accounts, for enforcing rights under Sarfaesi Act, consent of _ lenders is required.
*(a) 75% lenders by value (b) 60% lenders by number (c) Both (a) and (b) (d) None
50. For enforcing rights under SARFAESI Act, the action can be initiated by:
(a) Chief Manager & above (B) AGM & above (c) Senior Manager or above
*(d) Chief Manager & above or any authority approved by Board of Directors of the Bank
51.Which of the following is correct regarding enforcing rights under Sarfaesi Act?
(a) Minimum outstanding in the account should be Rs 1 lac or above
(b) Possession of security can not be taken over if loan is raised for any agricultural purpose.
(c) Action can be taken even if limitation has expired
*(d) Objective of the Act is speedy recovery of NPAs (e) Both (a) & (b) only
52. Bank has initiated action under Sarfaesi Act. The borrower objects to bank's action. With whom, he can file application against the action of the bank, if the outstanding in the account is Rs 2,00,000.
(a) District Court (b) High Court *(c) DRT (d) DRAT (e) None of these
53. For selling goods acquired by enforcing rights under Sarfaesi Act, days notice is to be given to the borrower/guarantor:
*a) 30 (b) 45 (c) 90 (d) 60 (e) 120
54. If a borrower makes a representation to bank against action taken by bank under Sarfaesi Act, bank is
required to reply with in _____ days.
a) 30 (b) 45 lc) 7 (d) 60. (e) 120
55. A borrower who wants to file an application with DRT in respect of action initiated by the bank under SARFAESI Act, 2002 is required to deposit with DRT
(a) 50% of the amount due to the bank (b) 75% of the suit amount due to the bank

(c) 50% of the amount due to the bank which can be reduced to 25% by the Presiding Officer
(d) 25% of the amount due to the bank *(e) No amount to be deposited.
56. The validity of the SARFAESI Act was challenged before Supreme Court in the case of :
(a) Union of India versus Mardia Chemicals Ltd *b) Mardia Chemicals Ltd versus Union of India & Others
c) Mardia Chemicals Ltd versus ICICI Bank d) Mardia Cements Ltd versus ICICI e) None of these
57. For making appeal to DRAT, under SARFAESI Act, the borrower is required to deposit _of the dues which can be reduced to _____ by the DRAT.
a) 75%, 0% b) 50%, 0% *c) 50%, 25% d) 75%, 25% e) None of these
58. As per decision of Supreme Court in the case of_____ , bank can take action simultaneously under Sarfaesi and also file case with DRT or normal court for recovery.
(a) Union of India versus Mardia Chemicals Ltd b) Mardia Chemicals Ltd versus Union of India & Others
*c) Transcore Ltd versus Union of India & others d) None of these
59. An account will be eligible for Corporate Debt Restructuring if:
a) the limit has been availed from more than one bank b) minimum outstanding is Rs 10 crore
c) account is standard, sub standard or doubtful d) Only (a) & (b) *e) All of these
60. When an account is restructured, it will be upgraded after 12 months from the due date of first instalment
provided instalments are paid regularly for _____ after restructuring.
a) 3 months b) 6 months *c) 1 year d) 2 year e) None of these
61. An account will be eligible for Corporate Debt Restructuring if:
a) the loan has been raised by corporate i.e. limited company or co-operative society
b) the loan has been raised for manufacturing or any other activity
c) no fraud is involved *(d) all of these (e) None of these
62. Which of the following is not correct regarding CDR?
(a) CDR Il is applicable to Doubtful accounts *(b) CDR is applicable to all type of NPA
(c) Proposals under CDR I can be referred if 20% of lenders by value agree. (d) None of these
63. CDR 1 is applicable to:
a) Standard accounts (b) sub standard accounts (c) Doubtful accounts *d) Both (a) and (b)
64. Which of the following factors is not taken into account while considering a proposal for CDR?
(a) Return on capital employed (b) gap between internal rate of return and cost of funds
(c) Debt Service Coverage Ratio (d) extent of sacrifice *(e) None of these
65. Which of the following is the main criteria for decision relating to restructuring of a unit?
— (a) unit should be able to become viable in 7 years (b) restructured debt should be paid within 10 years
(c) unit should be able to become viable in 5 years *(d) Both (a) & (b) (e) Both (b) & (c)
66. Which of the following is not correct regarding eligibility under CDR?
(a) Minimum outstanding should be more than Rs 10 core
(b) CDR is available for single lender and multiple lender accounts
(c) Wilful defaulters can be considered if bank is satisfied *(d) Both (a) & (b) only
(e) All of these
67. Which of the following conditions have to be satisfied for SME being eligible for restructuring:
a) Account should be standard, sub standard or doubtful.
Outstanding balance is Rs 10 crore or below in case of advance by more than one bank to a corporate account became NPA not due to fraudd)Only (a) & (b), *e) All of these **(ANSWER IS - * MARKS)**

INTEREST RATES

t The monetary and credit policy statement of RBI is called:
*(a) Annual Policy Statement (b) Credit policy of RBI (c) Economic Policy (d) None of these
2. Base rate is fixed by:
(a) RBI (b) IBA (c) Ministry of Finance *(d) Asset Liability Management Committee of Bank
3. Interest rate on which of the following have not been deregulated by RBI and decided by RBI?
*(a) DRI (b) Ceiling rate on export credit (c) Ceiling rate on educational loans
(d) Both (b) and (c) only (e) All of these
4. The Working Group on BPLR headed by Mr Deepak Mohanty has suggested replacing BPLR with:

(a) Prime rate *(b) Base rate (c) Reference rate (d) Basis rate (e) None of these
5. What is the objective of introduction of Base Rate system in banks?
(a) Enhancing transparency in lending rates of banks
(b) Enabling better assessment of transmission of monetary policy
(c) To prevent monopoly and restrictive trade practices.
*(d) Both (a) and **(b)** only (e) All of these
Exposure Ceilings
6. The basic objective of prudential norms for exposure are:
(a) better risk management (b) avoidance of credit risk (c) higher profitability
*(d) Both (a) & (b) (c) All of these
7. In case of single borrowers, other than in infrastructure, the exposure ceiling is% of capital funds and for borrower group, the exposure ceiling is ____ % of capital funds.
*(a) 15%, 40% (b) 20%, 40% (C) 15%, 50% (d) 20%, 50%
8. Credit Exposure ceiling for borrowers is linked to:
(a) Paid up capital of bank (b) Net worth of bank *(c) Capital fund of the bank (d) None of these
9. For the purpose of exposure norms, what is the meaning of capital fund?
(a) paid up capital and reserves (b) Tier I capital *(c) Tier I & Tier II capital(d) None of these
10. In case of infrastructure projects, the exposure ceiling in case of individual borrowers is % of capital
funds and in case of borrower group it is _____ % of capital funds provided additional exposure is in respect
of infrastructure project.
(a) 15%, 40% (b) 20%, 40% (c) 15%, 50% *(d) 20%; 50% (e) None of these
11. How much additional exposure is permitted in exceptional circumstances with the permission of the Board of Directors of the bank in case of exposure to single borrower or group?
*(a)5%,5% (b) 10%, 10% (c) 5%, 10% (d) No additional exposure without RBI approval
12. Exposure norms are applicable to which of the following types of exposures?
(a) Credit facilities to weak/sick industrial units under rehabilitation packages (b) Food credit
*(c) Loans guaranteed by State Government (d) Both (a) & (b) only (e) None of these
13. Exposure norms are not applicable to which of the following?
*(a) Advance against Bank's own deposit (b) Advance against LIP (c) Advance against NSC
(d) Seasonal Industries .(e) All of these
14. For the purpose of exposure norms, which of the following is true for inclusion under exposure?
(a) 100% of both fund based and non fund based credit limits
(b) Sanctioned limit or outstanding whichever is higher shall be considered.
(c) In case of fully drawn term loans outstanding and not the limit sanctioned will be considered.
(d) Both (a) & (b) only *(e) All of these
15. For the purpose of exposure norms, what is the meaning of 'Group'?
(a) Majority of the directors should be common (b) The Managing Director should be same
*.(c) Commonality of Management and effective control (d) All of these
16. Which of the following is not treated as infrastructure for exposure norrhs?
(a) construction of cold storage for fruits, vegetables (b) laying down of gas pipeline •
(c) construction of educational institutions and hospitals *(d) None of these (e) Only (a) & (b)
. Capital Market Exposure
17. The aggregate exposure of a bank to the capital markets in all forms (both fund based and non-fund based)
on solo basis as well as consolidated basis should not exceed ____ % of its net worth as on March 31 of the previous year and the bank's direct investment in shares, convertible bonds / debentures, units of equity-oriented mutual funds and **all** exposures to Venture Capital Funds (VCFs) should not exceed _____% of its net worth.
(a) 20%; 40% (b) 15%; 40% *(c) 40%; 20% (d) 50%; 20% (e) None of these
18. As per Section 19(2) of the Banking Regulation Act, 1949, a banking company can hold shares in any company, whether as pledgee, mortgagee or absolute owner, up to:
(a) 30% of the paid-up share capital of that company

(b) 30% of paid-up share capital and reserves of the bank
(c) 30% of paid-up share capital and reserves of that company
*(d) (a) or (b) whichever is less (e) (a) or (c) whichever is less

19. Maximum advance from the banking system that can be allowed to an individual against shares, convertible bonds, convertible debentures and units of equity oriented mutual funds is restricted to:
(a) Rs.10 lakh if the securities are held in physical form
(b) Rs. 20 lakhs if the securities are held in demat form.
(c) Rs 20 lakhs whether securities are in physical or demat form
(d) Rs 10 lakhs whether securities are in physical or demat form *(e) Both (a) & (b) only
20. What is the minimum margin for financing against physical and demat shares?
(a) 50%, 25% *(b) 50%, 50% (C) 50%, 40% (d) 25%, 50% (e) None of these
21. How much minimum margin should be kept by banks while issuing guarantees on behalf of stock brokers or brokers in commodity exchange?
*(a) 50% of which cash margin should be minimum 25% (b) 25% with no sub limit for cash margin
(c) 100% of which cash margin should be minimum 50%(d) 50% with no sub limit for cash margin
22. Bank's investment in equity shares, Preference shares eligible for capital status, Subordinated debt
instruments, Hybrid debt capital instruments issued by other banks should not exceed_____% of the investing bank's capital funds (Tier I plus Tier II).
(a) 5% *(b) 10% (c) 15% (d) 20% (e) None of these
23. Banks have to limit their commitment by way of unsecured guarantees in such a manner that _of the bank's outstanding unsecured guarantees plus the total of outstanding unsecured advances do not exceed _____%of total outstanding advances.
(a) 10%, 15% (b) 15%, 20% (c) 15%, 40% (d) 20%, 50%
*(e) None of these as there is no such stipulation.
24. Banks can not grant advance against their own shares as per provisions of:
(a) Section 20 (1) of RBI Act (b) Section 19(2) of Banking Regulation Act
(c) RBI guidelines *(d) Section 20 (1) of Banking Regulation Act (e) None of these
Loans to Directors of Banks
25. Banks can not grant any loans or advances to any of its directors except as permitted by RBI. This is as per provisions of :
(a) Section 20 (1) of RBI Act (b) Section 19(2) of Banking Regulation Act
(c) RBI guidelines Id) Section 20 (1) of Banking Regulation Act (e) None of these
26. Banks can not grant loans to any of its directors against which of the following securities?
(a) Government Securities (b) Life insurance policies (c) bank's own deposit
*(d) shares (e) Both (c) & (d)
27. As per Section 20A of the Banking Regulation Act, 1949, whose permission is required for remitting in whole or in part any debt due to a bank by any of its directors, or any firm or company in which any of its directors is interested as director, partner, managing agent or guarantor, or any individual, if any of its directors is his partner or guarantor.
*(a) Reserve Bank (b) Board of Directors of the Bank (c) SERI (d) Company Law Board
(e) None of these as loan given to a director can not be remitted at all.
28. Upto how much amount loan can be sanctioned by appropriate authority within powers delegated to him to any relative of their own director or directors of other banks or relative of director of other bank?
(a) up to Rs 25 lakh (b) Rs 25 lakh and above *(c) Less than Rs 25 lakh
(d) None of these as loan'to relatives of bank's directors can not be granted without RBI permission
29. Which of the following is correct regarding loan to directors of other banks or relatives of directors of own bank or directors of other banks?
(a) In all cases, loan can be sanctioned by appropriate authority but it should be reported to Board of Directors of sanctioning Bank
(b) In all cases, loan can not be granted without sanction of the Board of Directors of lending Bank.
(c) Loan of Rs 25 Iakh and above can be granted only after obtaining sanction of the Board of

Directors of lending bank

(d) Loan of less than Rs 25 lakh can be sanctioned by appropriate authority but it should be reported to Board of Directors of sanctioning Bank le) Both (c) and (d)

Miscellaneous Instructions

30. Which of the following is not sensitive commodity for purpose of Selective Credit Control?

(a) food grains i.e. cereals and pulses (b) major oil seeds and oils thereof (c) raw cotton and kapas *(d) Tea and Coffee (e) None of these

31. Which of the following commodities are presently covered under stipulations of Selective Credit Control?

a) food grains i.e. cereals and pulses (b) major oil seeds and oils thereof (c) raw cotton and kapas *(d) Buffer stock of sugar with sugar mills, unreleased stocks of sugar with sugar mills (e) None of these

32. Which of the following is correct regarding RBI guidelines on various types of loans?

(a) Banks will not grant loan against partly paid shares

(b) Banks will not grant loan to partnership/proprietorship concerns against the primary security of shares and debentures.

(c) Banks cannot grant loans against CDs or buy-back their own CDs before maturity except in respect of CDs held by mutual funds *(d) All of these (e) Only (a) and (b)

33.Why RBI has advised banks to desist from sanctioning advances against FDRs, of other banks?

(a) Other bank will not mark lien of lending bank *(b) It may result in double financing

(c) There may be possibility of fake term deposit receipts being used for obtaining advance

(d) All of these (e) Only (a) & (b)

34. As per Fair Practice Code, in case of receipt of request for transfer of borrowal account, either from the borrower or from a bank/financial institution, which proposes to take- over the account, the consent or objection of the lender, if any, should be conveyed within ____ from the date of receipt of request.

*(a) 21 days (b) 15 days (c) 7 days (d) one month (e0 None

35. Which of the following is not correct?

(a) Banks may negotiate bills drawn under LCs, on 'with recourse 'or 'without recourse 'basis

*(b) Banks can not purchase/discount the bills drawn otherwise than under LC on 'without recourse 'basis

(c) Banks should not rediscount bills earlier discounted by non-bank financial companies (NBFCs) except in respect of bills arising from sale of light commercial vehicles and two / three wheelers.

(d) Banks can not negotiate bills drawn under LCs, on 'with recourse 'or 'without recourse 'basis

Loan system for delivery of bank credit

36. Loan Delivery System was recommended by Committee headed by

*(a) Rashid Jilani (b) N. Vaghul (c) K. Kannan (d) C Rangarajan (e) None of these

37. Working Capital Demand Loan was recommended by:

*(a) Rashid Jilani (b) N. Vaghul (c) K. Kannan (d) C Rangarajan (e) None of these

38. Loan Delivery System is applicable in case of borrowers enjoying :

*(a) working capital credit limits of Rs. 10 crore and above from the banking system

(b) working capital credit limits of Rs 10 crore and above from a bank.

(c) fund based limits of Rs 10 crore and above from the banking system

(d) fund based limits of Rs 10 crore and above from a bank. --

39_ As per RBI, for borrowers availing working capital credit facilities of Rs 10 crore and above from the banking system, the loan component should normally be____ % and cash credit component should be %.

*(a) 80%, 20% (b) 20%, 80% (c) 75%, 25% (d) 60%, 40% (e) None of these

40. Which of the following is true regarding freedom to banks in respect of Loan Delivery System?

(a) Banks can increase the cash credit component beyond 20% but up to a maximum of 50%.

(b) Banks can increase the 'Loan Component' beyond 80% but up to a maximum of 90%

*(c) Banks can increase the Loan component or cash credit component up to any limit.

(d) Both (a) & (b) only (e) None of these

41. Loan Delivery System is not applicable in respect of which of the following type of business activities?

(a) which are cyclical (b) which are seasonal (c) which have inherent volatility *(d) all of these

42. Loan Delivery System is not applicable in respect of which of following-type of facilities?

(a) Bill finance (b) export credit (c) sick units (d) seasonal industries *(e) all of these

43. Which of the following is not correct regarding Loan system of credit delivery?
(a) Interest on loan portion and cash credit portion of limit can be different.
(b) Security is common for Loan portion and Cash credit portion.
(c) Demand Loan can be paid in lump sum or in instalments (e) All of these *(e) None of these

Consortium Loans and Multiple Banking Arrangement

44. As per RBI guidelines, a bank must lend through a consortium when credit facilities are more than:
(a) Rs 5 crore (b) Rs 50 crore (c) Rs 100 crore *(d) None of these
45. When is it necessary for a bank to form consortium for lending a borrower though RBI has waived requirement for the same?
(a) When credit facilities are more than 15% of capital fund of the financing bank in case of single borrowers
(b) **When** credit facilities are more than 40% of capital fund of the financing bank in case of group.
(c) When financing an infrastructure project Id) Only (a) and (b) (e) All of these
46. Which of the following is correct about consortium financing by banks?
(a) Minimum number of consortium members should be 2 and maximum number should be 4.
(b) Every bank will have same asset classification
(c) Minimum share of a bank in the consortium should be 10%
*(d) The banks **will** have a pari passu charge on the securities charged to them.
47. At the time of granting fresh facilities, which type of declarations is to be obtained from the borrowers?
(a) that they are not availing credit facilities from other bank
(b) that they are not availing working capital facilities from other bank
*(c) details about the credit facilities already enjoyed by them from other banks (d) None of these
48. When a borrower has availed credit facilities from more than one bank, banks should exchange information about the conduct of the borrowers' accounts with other banks at least at_____ intervals.
(a) monthly *(b) quarterly (c) half yearly (d) yearly (e) None of these
49. In the case of existing lenders, **all** the banks may seek a declaration from their existing borrowers availing sanctioned limits of____and above regarding credit facilities enjoyed by them from other banks.
(a) Rs 1 crore *(b) Rs 5 crore (c) Rs 10 crore(d) None of these **(ANSWER IS - * MARKS)**

LATEST MOCK TEST -1

1) MUDRA is set up with a corpus ofand a credit guarantee corpus of Rs 3,000 crore.
a) Rs.15,000 Crore b) Rs. 20,000 Crore; c) Rs. 30,000 Crore d) Rs. 50,000 Crore
2) As per the new budget, Surcharge has been increased to ____ for individuals earning 1 crore and above annually and on firms with an annual income of Rs. 10 crore or more.
a) 10% b) 12% c) 14% d) 15%
3) The full form of GIFT City is:
a) Gandhinagar International Finance Tec-City ; b) Gujarat International Finance Tec-City
c)Gujarat Indian Financial Tec-City ; d) Gandhinagar Indian Financial Tec-City
4) Full Form of CRILC City is:
a) Central Repository of Information on Large Credits
b) Central Reserve of Information on Large Credits
c) Central Repository of Information on ; e) None of the above
5) Full form of MIBOR;
a) Mumbai Inter bank Offered Rate
b) Mutual Inter bank Offered Rate
c) Mumbai International Offered Rate
d) Mumbai Inter bank Offer & Bid Rate
6) The limit of Education loan for vocational purpose in India for course duration for 3 to 6 months is _____:
a) 40,000b) 50000c) 60000 d) 75000
7) The limit of Education loan for vocational purpose in India for course duration of 6 months to 1 year is _____: a) 60,000 b) 85,000 c)1,00,000 d) 1,25,000
8) The limit of Education loan for vocational purpose in India for course duration above 1 year is :
a) Rs.1.5 lakh b) Rs. 2 lakh c) Rs.2.5 lakh d) Rs.3 lakh
9) Under SHG all the members of the group must be from BPL, however, a maximum of 20% in general and

30% in exception can be from marginally above poverty line subject to the condition that APL members not eligible for subsidy : a) 20%, 30% b) 25%, 35% c) 20%, 25% d) 15%, 25%

10) If the bank has raised an unauthorized/erroneous direct debit to an account and on verification of the entry it is found to be erroneous and the customer does not involve a third party, the bank will endeavor to complete the process of verification within a maximum period of _____ working days from the date of reporting of erroneous debit. In case, the verification involves a third party or where verifications are to be done at overseas centers, the bank shall complete the verification process within a maximum period of _____ month from the date of reporting of erroneous transaction by the customer.

a) 7 : one b) 5; one c)14; two d) 10; three

11) The Bank will undertake to carry out direct debit / ECS debit instructions of customers in time. In the event the bank fails to meet such commitments customer will be
compensated to the extent of____ on account of delay
in carrying out the instruction/failure to carry out the instructions.

a) Any financial loss the customer would incur ;b) Rs. 1000/- c) Rs. 2500/- d) Rs. 5,000/

12) Where it is established that the bank had issued and activated a credit card without consent of the recipient, the bank would not only reverse the charges immediately but also pay a penalty without demur to the recipient amounting to _____ as per regulatory guidelines in this regard.

b) a) Twice the value of charges reversed ;b) Thrice the value of charges reversed Value of charges reversed

c) None of these

13) In case a cheque has been paid after stop payment instruction is acknowledged by the bank, the bank shall reverse the transaction and give value-dated credit to protect the interest of the customer. Any consequential financial loss to the customer will be compensated. Such debits will be reversed within ____ working days of the customer intimating the transaction to the bank

a) 3 b) 5 c) 2 d) 7

14) The bank will compensate the customer for undue delays in affording credit once proceeds are credited to the Nostro Account of the bank with its correspondent. Such compensation will be given for delays beyond
week / weeks from the date of credit to Nostro Account/ due date after taking into account normal cooling period stipulated. The compensation in such cases will be worked out keeping in view interest for the delay in crediting proceeds and compensation for any possible loss on account of adverse movement in foreign exchange rate. : a) One b) Two c) Three d) Four

15) As part of the compensation policy of the bank, the bank will pay interest to its customer on the amount of collection instruments in case there is delay in giving credit beyond the time period specified in banks cheque collection policy. Interest for delayed collection shall be paid at the Savings Bank rate for the period of delay beyond ____, ____, days as the case may be in collection of outstation cheques.

a) 5/10/15 b) 7/10/14 c) 3/5/7 d) none of these

16) The bank will pay interest to its customer on the amount of collection instruments in case there is delay in giving credit beyond 14 days. Interest will be paid at the rate applicable for term deposit for the corresponding respective period or Saving Bank rate, whichever is higher. In case of extraordinary delay, i.e. delays exceeding ____ days interest will be paid at the rate of ___% above the corresponding Term Deposit rate.

a) 60;2 b) 30;3 c) 90; 2 c) 45;2

17) In the event the proceeds of cheque under collection was to be credited to an overdraft/loan account of the customer, interest will be paid at the rate applicable to the loan account. For extraordinary delays, interest will be paid at the rate of ____above the rate applicable to the loan account.

a) 4% b) 3% c) 2% d) 2.5%

18) In line with the compensation policy of the bank, the bank will compensate the account holder in respect of instruments lost in transit. In case intimation regarding loss of instrument is conveyed to the customer beyond the time limit stipulated for collection_____, ____, _____ days as the case may be) interest will be paid for the period exceeding the stipulated collection period at the rates specified above.

a) 4/8/12 b) 5/10/15 c) 7/10/14 d) 6/10/13

19) Issue of Duplicate Draft and Compensation for delays Duplicate draft will be issued within a _____ from the receipt of such request from the purchaser thereof. For delay beyond the above stipulated period, interest at the
rate applicable for ___ of corresponding period will be
paid as compensation to the customer for such delay.

a) Fortnight; Fixed Deposit b) 10 days; Fixed Deposit

c) Fortnight; cumulative Deposit d) 30 days / Fixed Deposit

20) In addition, bank will pay interest on the amount of the
cheque for a further period of _____ days at Savings
Bank rate to provide for likely further delay in obtaining duplicate cheque / instrument and collection thereof.

a) 15 b) 10 c) 7 d) 12

21) Violation of the Code by banks agent In the event of receipt of any complaint from the customer that the bank's representative / courier or DSA has engaged in any improper conduct or acted in violation of the Code of Bank's Commitment to Customers which the bank has adopted voluntarily, the bank is committed to investigate the matter and endeavor to communicate the findings to the customer within _____ working days from the date of receipt of complaint and wherever justified, compensate the customer for financial loss, if any, as contemplated under this policy.

a) 10 b) 7 c) 12 d) 15

22) In terms of the guidelines for lenders liability, and the Code of Bank's Commitment to customers, the bank would return to the borrowers all the securities / documents / title deeds to mortgaged property within _____ days of repayment of all dues agreed to or contracted The bank will compensate the borrower for monetary loss suffered, if any due to delay in return of the same. In the event of loss of title deeds to mortgage property at the hands of the banks the compensation will cover out of pocket expenses for obtaining duplicate documents plus a lump sum amount as decided by the bank.

a) 7 b) 15 c) 21 d) 25

23) It is mandatory for bank to reimburse the customer, the amount wrongfully debited on account of failed ATM within a maximum period of _____ working days from the receipt of the complaint. For any failure to re-credit the customer's account within the stipulated period from the date of receipt of the complaint, bank shall pay compensation of Rs._____ - per day to the aggrieved customer. This compensation shall be credited to the customer's account automatically without any claim from the customer, on the same day when bank affords the credit for the failed ATM transactions.

a) 5;100 b) 10;150 c) 14;150 d) 7;100/

24) Which of the following statement is incorrect?

a) The bank will not honour cheques drawn on current accounts maintained by other banks with it unless arrangements are made for funding cheques issued. Issuing bank should be responsible to compensate the cheque holder for non payment / delayed payment of cheques in the absence of adequate funding arrangement.

b) The Bank would not compensate the customer for delays in collection of cheques designated in foreign currencies sent to foreign countries as the bank would not be able to ensure timely credit from overseas banks.

c) In the event a cheque or an instrument accepted for collection is lost in transit or in the clearing process or at the paying bank's branch, the bank shall immediately on coming to know of the loss, bring the same to the notice of the account holder so that the account holder can inform the drawer to record stop payment and also take care that cheques, if any, issued by him / her are not dishonoured due to non-credit of the amount of the lost cheques / instruments. The bank would provide all assistance to the customer to obtain a duplicate instrument from the drawer of the cheque.

d).The bank would not compensate the customer for any reasonable charges he/she incurs in getting duplicate cheque / instrument upon production of receipt. The instrument is to be obtained from a bank/ institution who would charge a fee for issue of duplicate instrument.

25) The Reserve Bank has set out a five-pillar framework to guide its developmental and regulatory measures. Which of the following is not the regulatory pillar:

a) PILLAR – I: Clarifying and strengthening the monetary policy framework.

b) PILLAR – II: Strengthening banking structure through new entry, branch expansion, encouraging new

varieties of banks, and moving foreign banks into better regulated organisational forms.
c)PILLAR – III: Broadening and deepening financial markets and increasing their liquidity and resilience so that they can help absorb the risks entailed in financing India's growth.
d) PILLAR – IV : Expanding access to finance to small and medium enterprises, the unorganised sector, the poor, and remote and underserved areas of the country through measures to foster financial inclusion.
e) PILLAR – V: Improving the system's ability to deal with
corporate distress and financial institution distress by
strengthening real and financial restructuring as well as debt recovery.
f) None of the above
26) Which pillar of RBI's developmental and regulatory measures emphasizes on Strengthening banking structure through new entry, branch expansion,
encouraging new varieties of banks, and moving foreign banks into better regulated organisational forms.
a) Pillar I b) Pillar III c) Pillar II d) Pillar V
27) Which pillar of RBI's developmental and regulatory measures emphasizes expanding access to finance to small and medium enterprises, the unorganised sector, the poor, and remote and underserved areas of the country through measures to foster financial inclusion.
a) Pillar I b) Pillar IV c) Pillar II d) Pillar V
28) On a review of the permitted transactions under the Rupee Drawing Arrangements (RDAs), the Reserve Bank increased the limit of trade transactions from the existing Rs.5,00,000/- per transaction to Rs._____ per transaction, with immediate effect. a) 10,00,000 b) 12,00,000 c) 15,00,000 d) 17,50,000
29) The concept of a _____ account was introduced in the current framework as an important step in fraud risk control.
a) Special Mention account. b) Red Flagged
c) High Risk account. d) Early Mortality account.
30) A ___ is one where suspicion of fraudulent activity
is thrown up by the presence of one or more Early Warning Signals (EWS).
a) Red Flagged Account b) Special Mention account.
c) High Risk account. d) Early Mortality account.
31) The threshold for Early Warning Signals and Red
Flagged Account is an exposure of ____or more at the
level of a bank irrespective of the lending arrangement (whether solo banking, multiple banking or consortium).
a) 100 millionb) 250 million c) 500 million d) 1000 million
32) The officer responsible for the operations in the account should be sensitized to observe and report any manifestation of the Early Warning Signal promptly to the
_____ or any other group constituted by the bank
for the purpose immediately.
a) Fraud Monitoring Group (FMG)
b) Fraud Management Group (FMG)
c) Core Monitoring Group (CMG)
d) Fraud Surveillance Group (FSG)
33) The Framework for fraud risk management in banks also includes broad guidelines relating to the, which of the following?
(i) Reporting to the Central Repository of Information on Large Credits (CRILC).
(ii) Lending under consortium or multiple banking arrangements
(iii) Staff accountability.
(iv) Filing complaints with law enforcement agencies.
(v) Penal measures for fraudulent borrowers
(vi) Central Fraud Registry.

a) (i) & (ii) only b) (iii) to (vi) only

c) All of the above d) None of these

34) The Reserve Bank has advised all public sector banks and select private sector and foreign banks to appoint an internal Ombudsman. The internal Ombudsman would be designated as_____ :

a) Chief Ombudsman Service Officer

b) Chief Customer Ombudsman Officer

c) Internal Ombudsman Customer Service Officer

d) Chief Customer Service Officer

35) The Reserve banks has directed all _____ and few _____ to appoint Chief Customer Service Officers. (Internal Ombudsman).

a) Public Sector Banks; Private Sector & Foreign Banks

b) Private Sector Banks; Foreign Banks

c) Private Banks & Foreign Banks

d) Private Sector Banks; Public Sector Banks

36) As per the revised norms, the procedures for acquisition of accommodation on lease / rental basis by all commercial banks will now be determined by the_____ :

a) State Govt. b) RBI

c) Banks themselves d) Ministry of Finance

37) Which committee has prescribed seven broad themes to the Reserve Bank to advise all public sector banks to suitably determine the agenda items and the periodicity thereof, keeping in view that there is adequate focus on matters of strategic and financial importance?

a) Kamath Committee. b) Urjit Patel Committee

c) Nayak Committeed) Nachiket Mor Committee.

38) The Reserve Bank had, in the first bi-monthly monetary policy statement 2015-16, proposed to do away with the _____ and instead, replace it with the seven critical themes.

a) Monitoring of critical areas b) Calendar of Reviews

c) Monitoring of strategic assets

d) Calendar of performance parameters

39) The seven themes include business strategy, financial reports and their integrity, risk, compliance,_____, _____and human resources.

a) Customer protection, Financial inclusion

b) Customer awareness, Financial integrity

c) Customer awareness, Fraud management.

d) Strategic Marketing, Financial inclusion

40) In order to enable private sector banks to attract and retain professional directors, the Reserve Bank has issued guidelines on compensation for non-executive Directors for implementation by private sector banks, that will reflect market realities and will be within the parameters specified in the:

a) Banking Regulation Act, 1949b) The Companies Act, 2013

c) Both of these d) None of these

41) The Board may, at its discretion, provide for in the policy, payment of compensation in the form of____ to

the non-executive directors (other than the Part-time Chairman), subject to the bank making profits.

a) Bonus b) Commission on profits

c) Additional Shares d) None of these

42) Such compensation, however, shall not exceed _ per annum for each director.

a) 1 million b) 1.5 million c) 0.5 milliond) 2 million

43) In addition to the directors' compensation, the bank may pay____ to the non-executive directors and reimburse their expenses for participation in the Board and other meetings.

a) Sitting fees b) Commission

c) Bonus d) Additional allowances

44) Banks in private sector would be required to obtain prior approval of the Reserve Bank for granting ____ to the part-time non-executive Chairman. a) Bonusb) Commission c) Remuneration d) Loans

45) The compensation policies of banks would be subject to supervisory oversight including review under the Supervisory Review and Evaluation Process (SREP) under framework.

a) Pillar 2 and Basel III framework ; b.Pillar 3 and Basel III framework ; c.Pillar 2 and Basel II framework

d. Pillar 1 and Basel II framework

46) Banks are required to make disclosure on remuneration paid to the directors on an _____ basis at the minimum, in their Annual Financial Statements.

a) Semi annual b) Quarterly c) Monthly d) Annual

47) Under the revised criteria for opening of branches / extension counters / specialised branches within the area of operation of the StCBs, Capital to Risk (Weighted) Assets Ratio (CRAR) should not be less than_____:

a) 9 percent b) 10 percentc) 8 percent d) 10.5 percent

48) Under the same revised criteria, net Non Performing Assets (NPA) should be less than _____:

a) 9 percent b) 5 percent c) 8 percent d) 6 percent

ANSWER

1	B	2	B	3	B	4	A	5	A
6	B	7	D	8	A	9	A	10	A
11	A	12	A	13	C	14	A	15	B
16	C	17	C	18	C	19	A	20	A
21	B	22	B	23	D	24	D	25	F
26	C	27	B	28	C	29	B	30	A
31	C	32	A	33	C	34	D	35	A
36	C	37	C	38	B	39	A	40	C
41	B	42	A	43	A	44	C	45	C
46	D	47	A	48	B				

LATEST MOCK TEST - 2

01 Which of the following is not true about Equitable Mortgage?

a) It is created by Deposit of title deeds.

b) Title Deeds can be deposited by Mortgagor or his authorized agent.

c) Title Deeds can be deposited at Mumbai, Kolkatta, Chennai or any other place notified by State Government.

d) It can be only in respect of property located in urban areas

02 What is the gurantee fees payable under CGTMSE for loans up to Rs 5 lac in North East or to a woman?

a) 0.5% of the limit sanctioned.

b) 0.75% of the limit sanctioned as on 31st March.

c) 0.75% of the amount outstanding as on 31st March.

d) 1% of the outstanding amount as on 31st March.

03 A manufacturing enterprise will be classified as small enterprise, if original investment in plant and machinery is up to____.
a) Rs 10 lakh b) Rs 25 lakh
c) Rs 2 crore d) Rs 5 crore

04 Validity period of a cheque is considered as three months as per provisions of which of the following?
a) N I Act b) R B I Act
c) Banking Regulation Act d) As per practice
e) As per RBI guidelines

05 The maximum amount of compensation that can be awarded by an Ombudsman in case of other than Credit Cards is restricted to ____ .
a) Rs 5 lakh b) Rs 10 lakh
c) Rs 1 lakh d) Rs 50 lakh

06 Which of the following is not true about application of Garnishee order?
a) Garnishee order issued in single name is not applicable on the credit balance in joint accounts.
b) Garnishee order is applicable only on the amount available with the bank at the time of receipt of Garnishee order and not on the amount deposited after receipt of Garnishee order.
c) Garnishee order is applicable on Debts Due as well as Debts accruing Due.
d) Garnishee order is applicable on Cash credit account to the extent of unutilized limit provided it is within Drawing power.

07 In a loan granted to an individual who is major, guarantee was obtained from a Minor. It was pointed out by Auditors that minor could not enter into a contract and guarantee given by minor is invalid. Now the minor has become major and is prepared to ratify the contract of guarantee. What is the position regarding liability of the minor who has now become major?
a) Minor will be liable but only for transactions carried out after ratification by him.
b) Minor will be liable for all transactions from the date he signed guarantee document.
c) Minor will not be liable as minor can not ratify contracts entered into by him during minority.
d) Minor can ratify the contract provided consent is also obtained from his guardian

08 Which of the following can not be a partner? a) Hindu Undivided Family b) Partnership Firm
c) Limited Company d) Major person

09). For the purpose of Asset Classification, what is the status of accounts, where outstanding balance in the principal operating account is less than the sanctioned limit/drawing power, but there are no credits continuously for 90 days as on the date of Balance Sheet or credits are not enough to cover the interest debited during the same period?
a.These accounts should be treated as 'out of order'.
b.These account should be treated as NPA.
c.These accounts will be treated as NPA only if these remain out of order for 6 months.
d.These accounts will be treated as Sub standard. & e. None of these

10.Which of the following accounts can be opened jointly with residents as well as non residents?
a. Non Resident Ordinary ; b.Non Resident External ; c.Foreign Currency Non Resident Account
d. None of these ;e. All of these.

11.Which of the following represents feature of Deferred Payment Guarantee?
a.It is a method of financing long term debt just like cash credit but without directly extending the loan. In b. DPG, the advantage to the buyer of machinery is that he benefits to the extent of savings in interest charges accruing on account of opting for equipment financing plus the guarantee charges paid to the bank.
c.For the buyer of the plant and machinery, DPG serves the same purpose as term loan.
d.Deferred Payment Guarantee is a Contingent Liability and therefore can not be treated as method of financing long term debt.

12 What is the due date of a bill dated 12th June 2015 payble two months after date sighted on 14th June and accepted on 16th June. a).14th August 2015; b) 15th August 2015; c). 16th August 2015;
d) 17th August 2015 ; e).19th August 2015

13.To be eligible for raising loan under PMEGP, the annual family income of the beneficiary should not be more than___a.Rs 100,000 b)Rs.200,000 ;c) minimum prescribed for Below poverty line.

d).None of these as there is no income ceiling.

14.The number of members in a Joint Liability Group should be ___a) 4 to 10 b) 10 to 25
c) 10 to 20 d) 5 to 10

15. A Sub-Committee of the Central Board of the Reserve Bank was constituted to study issues and concerns in the MFI sector under the chairmanship of : a) Ms Usha Thorat b) Shri Y. H. Malegam
c) Ms Shyamala Gopinath d) Shri Anand Sinha

16 In the case of banks, deposits are insured by which of the following? :

a) Deposit Insurance Company Ltd.
b) National Deposit Insurance Company Ltd.
c) Deposit Insurance and Credit Guarantee Corporation Ltd.
d) Indian Deposit Insurance Company Ltd. ; e) None of these

17 When advance is granted against Life Insurance Policy, charge is created by way of .
a) Lien b) Pledge ; c) Hypothecation d) Assignment ; e) Mortgage

18 As per provisions of Indian Stamp Act, when duty is required to be paid in case of receipts and how much duty is payable?

a) When receipt is Rs 5000 or above and duty is Rs 1.
b) When receipt is Rs 500 or above and duty is Rs 1.
c) When receipt is more than Rs 5000 and duty is Rs 1.
d) When receipt is more than Rs 5000 and duty is Rs 2.

19 A cheque drawn on your branch has been presented for payment. The cheque is partly written in English, partly in Hindi and partly in the local language of the area in which the branch is located. If the cheque is otherwise in order, what would you do?

a) The cheque can be paid as a cheque can be written in any language.
b) The cheque could have been paid if it was either in Hindi or in English or a combination of both.
c) The cheque can not be paid as it is written in vernacular language.
d) The cheque can be paid as a cheque can be written in English, Hindi or vernacular language of the area where the buying branch is located.

20 For a remittance of Rs 100,000 under NEFT how much maximum charges other than service tax can be charged by a bank to the remitter? a) Rs 5 b) Rs 25 ; c) Rs 50 d) Rs 5 per thousand
e) None of these

21 IFSC or Indian Financial System Code is a 11 digit alpha-numeric code that uniquely identifies a bank-branch participating in the NEFT system. How many characters are alpha and how many characters are numeric in the code?

a) first 4 alpha characters representing the bank, and the last 6 numeric characters representing the branch and 5th character is 0.
b) first 4 alpha characters representing the branch and the last 6 numeric characters representing the bank and 5th character is 0.
first 5 alpha characters representing the bank, and the last 6 numeric characters representing the branch.
d) first 5 alpha characters representing the bank, and the last 5 numeric characters representing the branch and 6th character is 0.

22 Which of the following is not decided by RBI? a) Repo Rate b) Reverse Repo Rate
c) Bank Rate d) Inflation Rate

23 Which of the following concept has been implemented with effect from 1st July 2010?
a) Benchmark Prime Lending Rate : b) Base Rate c) Basis Rate; d) Bank Rate e) LIBOR

24 Under NEFT, settlement takes place in how many batches on Monday to Friday and in how many batches on Saturdays? a) 12; 6 b) 6; 3 c) 9; 5 d) 11; 5 e) None of these

25 What will be the Current Ratio if the following figures have been taken from the balance sheet of a firm? Stock 150, Debtors 175; Cash 75; preoperative expenses 50; sundry creditors 200; Bank borrowing for

working capital 100; Reserves 100. a) 1.33:1 b) 1.5:1; c) 1:1 d) 1.2:1

26 Which of the following is not considered as Agricultural advance (1) Advance to farmer for purchase of farm machinery (2) Loan to marginal farmer for purchase of agri land (3) Agri clinic and Agri Business Centre (4) Loan to dealer in poultry feed and cattle feed.
a) Only 4 b) Both 1 and 3 ; c) 1,3, and 4 d) All of these

27 With effect from 1st July 2010, interest rates of Banks are linked to which of the following?
a) Base Rate ; b) Benchmark Prime Lending Rate ; c) Bank Rate d) Repo Rate

28 Foreign Currency Non Resident (Bank) account can be opened for a maximum period of .
a) 1 year b) 3 year ; c) 5 year d) 7 year e) None

29 Banks are required to reimburse to the customers, the amount wrongfully debited on account of failed ATM transactions within a maximum period of _____ .
a) 7 days from the date of receipt of customer complaint.
b) 7 working days from the date of receipt of customer complaint.
c) 7 working days from the date of wrong debit receipt of customer complaint.
d) 12 days from the date of receipt of customer complaint.
e) None of these

30 Action under Sarfaesi Act can be taken by a bank in respect of which of the following types of advances?
b) a) Only Standard Assets Only Sub Standard Assets ; c) All NPAs ; d) All NPAs except loss accounts e)All NPAs except sub standard accounts

31 Royal Bank of Scotland based in London opens an account with State Bank of India in Mumbai in Indian Rupees. For SBI this account will be treated as : a) Nostro account b) Vostro account
c) Loro account d) None of these

32 The provisions relating to crossing are applicable to Cheques and Drafts only. In this regard, as per Negotiable Instruments Act, who can not cross a cheque? : a) Drawer of cheque b) Holder of Cheque ; c) Payee of Cheque d) Collecting Bank ;e) None of these

33 Which of the following is correct regarding Operating Hours of NEFT?
a) NEFT operates in hourly batches - there are twelve settlements from 8 am to 7 pm on week days and six settlements from 8 am to 1 pm on Saturdays.
b) NEFT operates in batches of 2 hours each – there are seven settlements from 9 am to 5 am on week days and five settlements from 9 am to 1 pm on Saturdays.
c) NEFT operates in batches of one hour and two hour – there are nine settlements from 9 am to 5 am on week days and three settlements from 9 am to 12 pm on Saturdays.
d) None of these

34 What is the relationship between customer and bank in the case of Safe Deposit Vault?
a) Lessor, Lessee b) Lessee, Lessor ; c) Bailor, Bailee d) Creditor, Debtor

35 For coverage under Priority Sector, how much maximum amount can be granted as educational loan for education in India and education abroad?
a) Rs 10 lakh, Rs 20 lakh ; b) Rs 10 lakh, Rs 10 lakh ; c) Rs 4 lakh, Rs 10 lakh
d)Rs 7.5 lakh, Rs 15 lakh & e) None of these

36 Balance Sheet of a firm indicates which of the following?
a) Profit or Loss over a period.
b) Financial position of the unit over a period.
c) Financial position of the unit as on a particular date.
d) Position of assets and liabilities over a period of time.

37 What is the maximum charge excluding service tax and time varying tariff that can be charged by a bank for remittance of more than Rs 5 lakh through RTGS?
a) Rs 25 b) Rs 50 ; c) Rs 100 d) None of these

38 As per RBI directives, the limit for not obtaining collateral security in case of advance to micro and small enterprises is Rs. a) Rs 1 lac ; b). Rs 2 lac; c). Rs 5 lac ; d).Rs 10 lac & e) Rs 25 lac

39 with effect from 1st April 2010, if PAN is not submitted by the depositor, and interest payable on term deposit during the financial year is more than Rs 10,000, tax will be deducted at source at the rate of_____ .

a) 10% in case of individuals and HUF and 20% in the case of companies.
b) 10% in case of all assesses.
c) 20% in case of all assesses.
d) Nil if the depositor submits declaration on Form 15G or 15H otherwise at the rate of 20%.

40 In the case of agricultural advances, banks shall not obtain collateral security for loans up to
a) Rs 25,000 b) Rs 50,000 ; c) Rs 100,000 d) Rs 200,000; e)None of these

41. In case of short term production credit to farmers up to Rs 3 lac, what is the rate of interest subvention for 2014-15? ; a)1.5% b) 2.5% ;c) 2% d) 3%

42. Interest on Saving Bank deposits is calculated on the basis of with effect from 1st April 2010.
a) Daily Product basis ; b) Minimum balance between 5th and last day of the month.
c) Minimum balance between 10th and last day of the month; d) Monthly Product basis

43. For making nomination, cancellation of nomination and variation in the case of deposits which forms are used? ; a) DA-1, DA-2, DA-3 ; b) DA-1, DA-3, DA-2 ; c) SC-1, SC-2, SC-3 d) SL-1, SL-2, SL-3

44.A customer uses which of the following types of cards for making purchases in the market when he wants to make payment later on? : a) Debit Card b) ATM Card ; c) Credit Card d) General Card

45.When a borrower does not avail his Cash credit limit fully, banks have the practice of charging some charge from him for the unutilized portion of the limit. This charge is called : a) Service Charge ;
b) Incidental Charge; c) Documentation Charge ; d) Commitment Charge

46.In the case of a fixed deposit in the name of an individual, in which nomination has been made, which of the following can be done by nomine the depositor dies before maturity of term deposit?

a) He can raise loan against FDR to meet the requirement of legal heirs.
b) He can make premature renewal of FDR.
c) He can take premature payment of FDR.
d) He can add the name of legal heirs in the FDR.

47 As per RBI guidelines, for depositing cheques for collection with the bank, both the drop box facility and the facility for acknowledgement of the cheques at regular collection counters should be available to the customers and no branch should refuse to give an acknowledgement if the customer tenders the cheques at the counters. Further, in the context of customer awareness in this regard, banks should invariably display a notice that "Customers can also tender the cheques at the counter and obtain acknowledgment on the pay-in-slips". The above message is required to be displayed at which place in the branch?

a) Outside the main entrance of the branch.
b) On the cheque drop-box itself.
c) In the customer lobby.
d) Any one of the places mentioned (a), (b) or (c).

48 What is the maximum loan amount that can be granted to SC/ST for housing under DRI scheme?
a) Rs 10,000 b) Rs 15,000 ; c) Rs 20,000 d) Rs 25,000 e) None

49 What is the amount of composite guarantee fee payable per annum under Credit Guarantee Scheme for Micro and Small Enterprise for loans more than Rs 5 lac if the loan is other than to a beneficiary in North East and Sikkim?

a) 0.75% of the limit sanctioned.
b) 1% of the limit sanctioned.
c) 1.5% of the limit sanctioned.
d) 0.85% of the limit sanctioned.

50 When can an agreement made by a minor for raising a loan be valid?

a) When loan is raised by misrepresenting the age.
b) When loan agreement is ratified on attaining majority.
c) When loan is guaranteed by somebody who is a major.
d) When loan is raised for a common purpose ; e) None of these

51 Which type of crossing restricts transferability of a cheque? a)Special Crossing; b)Not Negotiable Crossing ;c)Account Payee Crossing ; d) Both (b) and (c) only

52 What will be the net working capital if Current assets of a firm are Rs 500; Current Liabilities are Rs 300; Bank Borrowing is Rs 50. ; a) Rs 250 b) Rs 200 ; c) Rs 300 d) Rs 150

53 A Garnishee order issued against an individual account holder is not applicable in respect of which of the following? : a) Amount deposited after receipt of Garnishee order. ; b)Fixed deposit which is not due as yet.; c) Amount of a cheque purchased from the customer under Instant Credit Scheme.
d)Both (a) and (b) only ; e) Both (a) and (c) only.

54. Which of the following is not minority community as per guidelines issued by RBI?
a) Sikh b) Budhist c) Jain d) Only (a) and (b)e) None of these

55.As per Union Budget 2015-16, what is the rate of income tax chargeable to an individual having income more than Rs 250,000 but up to Rs 500,000 : a) 10%; b) 15% ;c)20% d) 30%

56. What is the object of Financial Inclusion? ; a) Providing banking facilities to unorganized labour only.
b) Providing banking facilities to Minority Communities and SC/ST; c) Providing banking facilities to students.d) Providing banking facilities to poor sections of society at affordable cost.

57. What rate of interest can be offered by banks in India on NRO term deposits?
a) As applicable in domestic term deposits.; b) As per Bank discretion.; c) As per Bank discretion subject to

the condition that it cannot be higher than those offered by the bank on comparable domestic rupee deposits.
d) None of these

58. RBI has advised banks to ensure that demand drafts of are issued invariably with account payee crossing. a)More than Rs 20,000 ;b) Rs 20,000 and above; c)Rs 50,000 and above
d). More than Rs 50,000

Answers

1	D	16	C	31	B	46	C
2	B	17	D	32	E	47	B
3	D	18	C	33	A	48	C
4	E	19	D	34	B	49	B
5	B	20	A	35	B	50	E
6	D	21	A	36	C	51	C
7	C	22	D	37	B	52	B
8	A	23	B	38	D	53	A
9	A	24	A	39	C	54	E
10	E	25	A	40	C	55	A
11	C	26	A	41	C	56	D
12	A	27	A	42	A	57	C
13	D	28	C	43	A	58	B
14	A	29	B	44	C		
15	B	30	C	45	D		

Basel-3 questions

01 RBI implemented the Basel-III recommendations in India, w.e.f: a) 01.01.2013, b. 31.03.2013, c. 01.04.2013, d. 30.09.2013

02 Basel III recommendations shall be completely implemented in India by:
31.03.2020, b. 31.03.2019 c. 31.03.2618 d. 31.03.2017

03 Basel III capital regulations were released by Basel Committee on Banking Supervision (BCBS) during as a Global Regulatory Framework for more resilient banks and banking systems:
December 2010, b. March 2011, c. December 2011, d. December 2012

04 Basel III capital regulations are based on 3 mutually reinforcing pillar. These pillars are (1) Pillar-1 minimum capital standards (2) supervisory review of capital adequacy (3) risk management.
all the 3 are correct, b. only 1 and 2 are correct, c. only 1 and 3 are correct, d. only 2 and 3 are correct
Under Basel II,

05.Under Basel II the option available to compute capital for credit risk are:-
standardized approach, b. risk management approach, c. advance measurement approach, d. standardized approach,
06. Under Basel III, the options available to compute capital for operational risk are :
standardized approach, b) risk management approach, c) advance measurement, approach, d) basic indicator approach,
07.Under Basel III, the options available to compute capital for market risk are :
standardized approach, b) risk management approach, c) advance, measurement approach, d) basic indicator approach
08.Certain specific prescription of Basel II capital adequacy framework will continue to apply along with Basel III (parallel run), till:
31.03.2019, b) 31.03.2018, c) 31.03.2017, d) 31.03.2016
09. A bank in India is to comply with capital adequacy ratio requirements at (1) consolidated (group) level after consolidating the assets liabilities of its subsidiaries / joint ventures (2) solo level (3) overseas operations of the bank under (I) and (2).
a)1 and 2 only correct, b) 1 and 3 only correct, c) 2 and 3 only correct, d) 1 to 3 all correct.
10. In India, the banks are required to maintain a minimum Pillar 1 capital to risk weighted assets ratio (or minimum total capital to risk weighted assets ratio) of a s o n
a) 8%, 31' Mar each year, b) 9%, 31" Mar each year, c) 8%, ongoing basis, d) 9%, ongoing basis.
11. The banks in India are required to compute Basel III capital ratios in the following manner (1) Common equity Tier I capital ratio (2) Tier I capital ratio (3) Tier 2 capital ratio (4) Total capital to risk weighted asset ratio a) I to 4 all, b) 1,2 and 4 only, c) 1, 3 and 4 only, d) 1 and 4 only
12. To calculate capital adequacy ratio, the banks are to take into account, which of the following risk:
credit risk and operational risk only, b) credit risk and market risk only, c) market risk and operational risk only, d) credit risk, market risk and operational risk.
13.Which of the following statement regarding the Total regulatory capital under Basel III is correct:
total regulatory capital is sum total of Tier I capital and Tier 2 capital, b) Tier I capital is called `aning-concern' capital and Tier 2 capital is called 'gone-concern' capital, c) Tier I capital comprises common equity Tier I and additional Tier I, d) all the above.
14 As per Basel III implementation in India, Common Equity Tier 1 capital must be % of risk weighted assets on ongoing basis: a: 5.5% b: 7%, c: 9% d: 11%
15. As per Basel III implementation in India, minimum Tier 1 capital must be % of risk weighted assets on ongoing basis:
a: 5.5% . b: 7%, c: 9% d: 11%
16. As per Basel III implementation in India, within the minimum Tier 1 capital, the additional Tier capital can be:
a: min 5.5% of risk weighted assets (RWA), b: max 5.5% of RWA, c: min 1.5% of RWA, d: max 1.5% of RWA
17. As per Basel III implementation in India, within total capital of 9% of risk weighted assets, the Tier 2 capital can be:
a: max equal to Tier I capital, b) min equal to Tier I capital c) max equal to 2% of risk weighted assets, d) min equal to 2% of risk weighted assets
18. Which of the following statements is not correct regarding Basel III implementation in India:
a) minimum common equity Tier I ratio should be 5.5% of RWAs, b) capital conservation buffer, c) (CCB) consisting of common equity, should be 2.5% of RWAs, d) maximum additional tier 1 capital should be 1.5% of RWAs, e) minimum common equity Tier I ratio plus capital conservation buffer should be 7%
19. Which of the following statements is not correct regarding Basel III implementation in India:
a) minimum Tier I capital ratio should be 8%, b) Tier 2 capital should be max 2%, c) minimum total capital ratio should be 9%, d) minimum total capital ratio plus capital conservation buffer should be 11.5%
20. As per Basel III, which of the following is an element of Common Equity component of Tier I (1) common shares i.e. paid up equity capital (2) stock surplus i.e. share premium (3) statutory reserves (4) capital reserves representing surplus arising out of sale proceeds of assets (5) balance in profit and loss account at the end of the previous year.
a) 1 to 5 all, b) I to 4 only, c) 1,4 and 5 only, d) 1, 2 and 3 only
21. As per Basel III, which of the following can be included in Additional Tier I capital (1) Perpetual Noncumulative Preference shares — PNCPS (2) stock surplus or share premium resulting from issue of Additional Tier I instruments (3) Debit capital instruments eligible to be included in additional Tier I.
a) 1 to 3 all, b) 1 and 2 only, c) 1 and 3 only, d) 2 and 3 only
22. As per Basel III, Tier 2 capital comprises which of the following (1) general provisions and loss reserves (2) debt

capital instruments issued by bank (3) preference share capital instruments with redeemable or cumulative feature (4) revaluation reserve (5) stock surplus i.e. share premium resulting from issue of Tier 2 eligible instruments.
a) 1 to 5 all, b) 1 to 4 only, c) 1, 4 and 5 only, d) 1, 2 and 3 only.
23. As per Basel III, general provisions and loss reserves are included in Tier-2 capital maximum to the extent of:
1.25% of total risk weighted assets under standardized approach and 0.6% of total risk weighted assets under IRB approach
a) 0.6% of total risk weighted assets under standardized approach and 0.6% of total risk weighted assets under IRB approach
b) 0.6% of total risk weighted assets under standardized approach and 1.25% of total risk weighted assets under IRB approach
c) 1.25% of total risk weighted assets under standardized approach and 1.25% of total risk weighted assets under IRB approach.
24 As per Basel III, the value of revaluation reserve is to be taken at % discount to include in Tier 2 capital:-
a: 60% b: 55%, c: 50% d: 45%
25 As per Basel III, adjustments / deductions are required to be made from Tier I and Tier 2 capital, relating to which of the following (1) goodwill and other intangible assets (2) deferred tax assets (3) Investment in own shares (treasury stock) (4) investment in capital of banking, financial or insurance entities :
1 to 4 all, b) 1 and 2 only, c) 1 and 3 only, d) 1 only
26 As per Basel III, the investment of a bank in the capital of a banking or financial or insurance entity is restricted to which of the following:
a) 10% of capital funds (after deductions) of the investing bank, b) 5% of the investee bank's equity capital, c 30% of paid up capital and reserves of the bank or 30%, of paid up capital of the company, whichever is lower. d all the above
27 The net stable funding ratio (NSFR) under Basel-III will be implemented in India from:
a 01.01.2017, b 01.04.2017, c 01.01.2018, d 01.04.2018
28. Under Basel III, the risk weight for capital charge for credit risk on the basis of standardized approach, does not match in respect of which of the following:
a. Fund & non-fund based claims on Central Govt. 0%, b Fund and non-fund based Central Govt. guaranteed claims — 0%, c Fund and non-fund based State Govt. guaranteed claims — 0%
D Fund and non-fund based claims on State Govt. — 0%.
29 Under Basel III, the risk weight for capital charge for credit risk on the *basis* of standardized approach, does not match in respect of which of the following:
a) Claims on RBI or DICGC 0%, b) Claims on Credit Guarantee Fund Trust for MSE — 0%, c) Claims on Credit Risk Guarantee Fund Trust for Low Income Housing — 0%, d) Claims on ECGC — 0%.
30. Under Basel III, the risk weight for capital charge for credit risk on the basis of standardized approach, does not match for claims on foreign governments (based on rating of international rating agencies such as S & P, Fitch, Moody's Rating), in respect of which of the following:
AAA to AA rating — 0%, b: BBB rating — 20%, c: Below B rating — 150%, d: unrated — 100%
31. Under Basel III, the risk weight for capital charge for credit risk on the basis of standardized approach, does not match for claims on foreign public sector enterprises (based on rating of S & P, Fitch, Moody's Rating), in respect of which of the following:
a: AAA to AA rating — 20%, b: A rating — 20%, c: BBB to BB rating — 100%, d: unrated — 100%.
32. Under Basel III, what is the risk weight for capital charge for credit risk on the basis of standardized approach, for claims on Bank for International Settlements, International Monetary Fund, Multi lateral Development Banks:
a: 0% b: 10%, c: 20% d: 50%.
33. Under Basel III, the risk weight is % for capital charge for credit risk on the basis of standardized approach, for claims on banks incorporated in India and foreign bank branches in India, where they meet the level of common equity Tier I capital and applicable CCB:
a: 0% b: 10%, c: 20% d: 50%
34.Under Basel III, the risk weight for capital charge for credit risk on the basis of standardized approach, does not match for claims on foreign banks (based on rating of international rating agencies such as S & P, Fitch, Moody's Rating), in respect of which of the following:
a) AAA to AA rating — 20% b) BBB rating — 50%, c) Below B rating — 150% d) unrated — 150%,
35. Under Basel III, the risk weight for capital charge for credit risk on the basis of standardized approach for long term loans, does not match for claims on domestic corporates, AFC and NBFC-IFC (based on

rating of internal rating agencies such as CRISIL, CARE, ICRA etc.), in respect of which of the following:
a) AAA rating — 20%, b) A rating — 50%, c) BBB —100%, d) unrated — 150%

36. Under Basel III, the risk weight for capital charge for credit risk on the basis of standardized approach for short term loans, does not match for claims on domestic corporates, AFC and NBFC-IFC (based on rating of internal rating agencies such as CRISIL, CARE, ICRA etc.), in respect of which of the following: a) Al+ - 20%, b) A2 — 50%, c) A3 — 75%, d) A4 — 150%

37. Under Basel III, the risk weight is % for capital charge for credit risk on the basis of standardized approach, for claims included in regulatory retail portfolio: a 20% b: 50%, c 75% d: 100%

38. Under Basel III, which of the following is part of the regulatory retail portfolio (1) mortgage loans which qualify as claim secured by residential property or commercial real estate (2) consumer credit or personal loans or credit card receivables (3) capital market exposure (4) venture capital exposure.
a) I and 3 only, b) 2 and 4 only, c) 1 to 4 all, d) none of the above

39. Under Basel III, to consider a claim as part of regulatory retail portfolio, which of the following condition is stated correctly: (1) orientation criteria i.e. the exposure to individual person or to small business, where total average annual turnover in small business is less than Rs.50 or (2) granularity criteria i.e. no aggregate exposure to one counterpart is more than 02% of overall regulatory retail portfolio (3) maximum retail exposure to one counterpart does not exceed the threshold limit of Rs. I cr.
a) 1 to 3 all, b) 1 and 2 only c) I and 3 only, d) 2 and 3 only

40. Under Basel III, the risk weight for capital charge for credit risk on the basis of standardized approach for home loan up to Rs.20 lac where loan to value (LTV) ratio is 90% is : a) 20% b) 50%, c) 75% d) 100%.

41. Under Basel III, the risk weight for capital charge for credit risk on the basis of standardized approach for home loan of above Rs.20 lac up to Rs.75 lac, where loan to value (LTV) ratio is 80% is : a) 20% b: 50%, c 75% d: 100%

42. Under Basel III, the risk weight for capital charge for credit risk as per standardized approach for home loan of above Rs.75 lac, where loan to value (LTV) ratio is 75% is :- a) 20% b: 50%, c 75% d: 100%

43. Under Basel III, the risk weight is for capital charge for credit risk on the basis of standardized approach for commercial real estate — residential housing: a) 20% b: 50%, c) 75% d: 100%.

44. Under Basel III, the risk weight is for capital charge for credit risk on the basis of standardized approach for exposure to commercial real estate:- 20% b: 50%, c: 75% d: 100%.

45. Under Basel III, for home loan purpose, the loan to value ratio (LTV) ratio is calculated as :
a) (principal + other charges) / (realizable value of mortgage property), b) (principal + accrued interest + other charges) / (realizable value of mortgage property) c) (principal + accrued interest) / (realizable value of mortgage property), d) (principal + accrued interest + other charges) / (cost of mortgage property)

46. Bank's exposure for dwelling unit to an individual shall be treated as exposure to commercial real estate, as per Basel III:- a: 2n^{d} b: 3rd, c 4th d: 5th

47. As per Basel III implementation, the risk weight for unsecured portion of NPA for credit risk as per standardized approach is % if the specific provision is less than 20% of the outstanding in NPA account:- 150% b: 100%, c: 75% d: 50%

48. As per Basel III implementation, the risk weight for unsecured portion of NPA for credit risk as per standardized approach is % if the specific provision is at least 20% of the outstanding in NPA account:- a 150% b: 100%, c: 75% d: 50%

49. As per Basel III implementation, the risk weight for unsecured portion of NPA for credit risk as per standardized approach is % if the specific provision is at least 50% of the outstanding in NPA account:- a 150% b: 100%, c: 75% d: 50%

50. Under Basel III, the risk weight for capital charge for credit risk on the basis of standardized approach for which of the following exposure, does not match: a) venture capital — 150% b) consumer credit or personal loans— 125%, c) credit card -125%, d) capital market exposure 100%

51. Under Basel III, the risk weight for capital charge for credit risk on the basis of standardized approach is

% for staff loans secured by superannuation benefits or mortgage of flat / house:
20% b:50%, c 75% d: 100%

52. Under Basel III, the risk weight for capital charge for credit risk on the basis of standardized approach is % for staff loans other than secured by superannuation benefits or mortgage of flat / house, being eligible under regulatory retail portfolio: a: 20% b: 50%, c 75% d: 100%

53. Under Basel III,under standardized approach, the total risk weighted off-balance sheet credit exposure is calculated by taking into account, the credit conversion factor (CCF). In which of the following, the CCF is not correctly stated: - a) direct credit substitutes such as financial guarantee or standby LC — 100%, b) performance guarantees 50%, c) self liquidating short term LC covering trading in goods — 50%, d) note issuance facilities and revolving underwriting facilities -50%

54. Credit enhancements under Securitization exposure, that are first loss positions, is to be risk weighted at _% under Basel III requirements:- A: 125% b: 375%, c: 625%, d: 1111%

55. Out of the following, which are domestic credit rating agencies, approved by RBI for the purpose of credit rating to determine risk weight for rated exposures (1) Brickwork (2) CARE (3) Fitch (4) CRISIL (5) Moody's (6) SMERA (7) Standard & Poor:- a 1, 2, 4, 7, b: 1, 2, 4, 6, c: 1,2 3,4, d: 1, 2, 4, 5

56 To be eligible for risk weighting purposes under Basel Ill, the rating from a credit rating agency approved by RBI, should be in force and confirmed from the monthly bulletin of the concerned rating agency. The rating agency should have reviewed the rating at least once during the previous months. A 6 months, b: 9 months, c: 12 months, d: 15 months

57. Under Basel III, which of the following are eligible as collateral for credit risk mitigation purpose: (1) cash (2) gold (3) Central or State Govt. securities (4) Kissan Vikas Tatra or National Saving Certificates (5) Life insurance policies and units of mutual funds (6) debt securities rated or unrated.
a: 1 to 6 all, _ b:A 2 to 6 only, cz to 5 only, dt 3 to 5 only

58. As per Basel HI requirements, modified by RBI, call option on Additional Tier 1 instrument (PNCPS and PDI) will be permissible at the initiative of the issuer after the instrument has run for at least years. a) two years b) three years c) five years d) ten years

59. As per Basel III, the risk of losses in on-balance shee and off-balance sheet positions arising from movements in market prices is called :- a) credit risk, b) market risk, c) pricing risk, d) liquidity risk

60. The market risk positions, that are subject to capital charge requirement, includes which of the following positions, under Basel III: a) risk pertaining to interest rate related instruments in the trading book, b) risk pertaining to equities in the trading book, c) forex risk including open positions in precious metal d) all the above.

61. The trading book of a bank is subject to market risk. As per Basel III, which of the following is not included in the trading book for capital adequacy purpose:- securities under HFT and AFS, b) open gold positions and forex positions, c) trading positions in derivatives, d) securities under HTM

62. If a security has matured and remains unpaid, it attract capital for risk on completion of 90 days delinquency period:- credit risk, b: market risk, c: operational risk, d: at discretion of the bank

63. For market risk, the minimum capital requirement is expressed in terms of two separately calculated charges which are:- a) specific risk and general market risk, b: special risk and general risk, c: liquidity risk and liquidation risk, d) counterparty credit risk and trading partner's risk.

64. The capital requirement for general market risk is designed under Basel III to capture the risk of loss arising from change in :- a prices of securities, b: market value securities, c: interest rate on securities, d: all the above

65. The capital charge for specific risk under market risk will be % or capital charge in accordance with the risk warranted by external rating of the counterparty, whichever is higher, under Basel HI. A: 9.00%, b: 9.75%, c: 10.50%, d: 11.25%

66 The capital charge for general market risk under the market risk will be % on gross equity

position, under Basel HI.

a: 9.00%, b: 9.75%, c: 10.50%, d: 11.25%

67. Under Basel III, the risk weight for open foreign currency and open gold position is:-

a: 50% b:75%, c: 100% d: 125%

68. The capital charge (CAR) for open foreign exchange positions and open gold positions, under Basel HI, for market risk is:- a 6% b: 7%, c: 8% d: 9%

69. The aggregate capital charge for market risk is the sum total of capital charge for (1) interest rate (2) equity investment (3) forex and gold open positions:- a) 1 to 3 all, b) 1 and 3 only, c) 1 and 2 only, d) 2 and 3 only

70. Under Basel Ill, the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events is called :- a) credit risk, b) operational risk, c) market risk, d) reputation risk

71. As per Basel III, which of the following is part of operational risk :- a) legal risk, b) reputational risk, c) strategic risk, d) all the above.

72. Under Basel HI, by using the Basic Indicator Approach, banks must hold capital for operational risk equal to the average over the previous years of a fixed percentage (denoted as alpha) of positive annual gross income. a) 2 years, b) 3 years, c) 5 years, d) at bank discretion

73. Under Basel III, by using the Basic Indicator Approach, banks must hold capital for operational risk equal to the average over the prescribed no. of previous years, at % (denoted as alpha) of positive annual gross income. a: 8% b: 9%, c: 12% d: 15%

74. For the purposeof calculation of capital charge for • operational risk under basic indicator approach, the gross income means:- a net interest income, b: net non-interest income, c: net interest income + net non-interest income, d: net interest income minus net non-interest income.

75. For the purposeof calculation of capital charge for operational risk under basic indicator approach, the gross income means:- a net profit + provisions and contingencies, b: net profit + provisions and contingencies + operating expenses, c net profit + operating-expenses, d: provisions and contingencies + operating expenses.

76 The risks that the banks are generally exposed to and are not captured or not fully captured in regulatory CRAR include which of the following:- a settlement risk, liquidity risk, b: reputational risk, strategic risk, c: risk of under-estimation of credit risk under standardized approach, d: all the above.

77. Under Pillar-2 of Basel III, the banks are required to have a Board approved ICAAP and assess capital accordingly. ICAAP stands for:

a: Internal Capital Adequacy Assessment Procedure, b) Internal Capital Approval Assessment Process

a) Internal Capital Adequacy Assessment Process, d) Internal Capital Assessment Approved Process

78. As per Basel III requirements, modified by RBI during Sept 2014, banks can issue Tier 2 capital instruments with a minimum original maturity of at least years.

a two years, b three years, c five years, d ten years

Risk Management Questions

79 Which of the 'following better explains the meaning of risk :- a loss arising on happening of some event, b loss arising on non-happening of some event, c probability of loss that could arise due to uncertainty, d probability of risk that could arise due to uncertainty, e risk due to loss as a result of uncertainty

80 Market risk is the risk of loss in (a) on-balance sheet positions (b) off balance sheet positions (c) arising from movement in market prices:- a a to c all are correct, b only a and c correct, c only b and c correct, d only a and b correct

81 Risk that is associated with inability/failure of banks in payment of amount representing clearing cheques presented by different banks:- a liquidity risk, b settlement risk, c credit risk, d legal risk e clearing process risk.

82. Risk that could arise due to legal actions or uncertainty of interpretations of contracts and agreements is called:- a) legal risk, b) contract risk, c) country risk, d) uncertainty risk, e) counter-party risk

83. A bank finds it difficult to repay the short term deposits on maturity to its deposits because the funds of the bank are locked in long term loans or investments. The risk arising from this situation is called:
a Interest rate risk, b Liquidity risk, c Operational risk, d Market risk, e Credit risk.

84. When failure of the financial system affects other systems such as insurance market or forex market, such risk is:- a liquidity risk, b settlement risk systemic risk, d systematic risk, e clearing process risk

85 Market risk takes the form of (which one is not correct):- a commodity price risk, b interest rate risk c loan default risk d liquidity risk.

86 The risk that loss may arise on account of trading in SLR and other securities by a bank is classified as:
a credit risk, b investment fluctuation risk c trading risk, d operational risk, e market risk

87. The risk that the interest rate of different assets and liabilities may change in different magnitude iscalled? A) Embedded Risk, b) Maturity Risk, c) Basis Risk, d) Price Risk

88. Exposure to uncertainty in economic value of *an* investment that could not be marked to market is called:- a) trading risk, b) business risk, c) market risk, d) liquidity risk, e) investment risk,

89. A foreign exchange dealer forgets to square the over bought position in a foreign currency. It is a..
a) foreign exchange risk, b) settlement risk, c) liquidity risk, d) operational risk

90. Risk that is associated with failure of internal processes of a bank or business organization:
a) settlement risk, b) procedural risk, c) operational risk, d) credit risk

91. A bank has failed to meet its obligation on account of a payment on due date due to its incapacity to pay. What kind of risk it is:
a) credit risk, b) liquidity risk, c) settlement risk, d) payment risk, e) all the above

92. Risk associated with changes in the credit profile of the borrowers and counter parties, is called:
a) credit risk, b) market risk, c) counter-party risk, d) liquidity risk, e) a and b –above

93. The customer service in a bank branch, has been disrupted for 2 hours, due to failure of the central server. What type of risk it is:
a reputation risk, b systemic risk, c operational risk, d settlement risk

94. When the bank is selling 3rd party products, which type of risk is involved:- a reputation risk, b operational risk, c credit risk, d liquidity risk e Financial Sector Terms

95 When the objective is to follow the best practices to conduct the affairs of a company or bank in a transparent manner for giving fair deal to all the stake holders, this is called:
a implementation of prudential guidelines, b organisational restructuring, c corporate governance, d corporate restructuring, e autonomy

96 Replacement of relatively high -cost debt with that of lower cost borrowing to take advantage of falling interest rates is called:
a debt replacement, b derivative, c credit enhancement, d credit risk management, e debt swap

97 In capital market, the term 'Market cap' is the product of a market price *x* authorised capital, b market price x paid up capital, c market price x outstanding no. of shares, d market price x shares e b and d

98. A banking system under which the banks are to raise low cost funds and invest such funds in low risk assets such as govt. securities, is known as:
a) narrow banking, b) universal banking, c) rural banking, d) risk management banking asset liability management banking

99. An entity established or incorporated outside India which proposes to make investment in India and which is registered as such, in accordance with the SEBI Regulations is called:
a) Indian Depository Receipt b) Foreign Institutional Investor c) Foreign Direct Investment, d) Foreign Currency
Convertible Bond

100. market provides a platform for trading of existing securities and price discovery thereof:
a) primary market, b) secondary market, c) money market, d) insurance market

101. Red Herring Prospectus is issued by a for a) company, to raise funds through

commercial paper, b) company, to raise funds from bank for a long term project, c) company, to raise capital from market under book building process in which the price of the share is not disclosed., d) bank, to raise funds from the overseas lenders.

102. An investment by non-resident entity/person resident outside India in the capital of an Indian company on a long term basis, is called :- a Indian Depository Receipt, b Foreign Institutional Investment, c Foreign. Direct Investment

D ForeignCurrency Convertible Bond

103.What is an Indian Depository Receipt?

a) deposit account with a public sector bank, b) A depository account with any of Depositories in India c) An instrument in the form of depository receipt created by an Indian depository against underlying equity shares of the issuing company, d An instrument in the form of deposit receipt issued by Indian depositories

104. When Reserve Bank injects liquidity in the monetary economy of the country, this is done through which of the following mechanisms?

a) increase in CRR, b) repo, c) increase in SLR, d) change in bank rate, e) liquidity adjustment facility

105. The receivables of various loans and obligations are put together and distributed amongst investors through marketable securities, in which of the following: a) leasing, b) factoring, c) securitization, d) venture capital, e) forfeiting

106. The process in which the electronic holding of share replaces the paper securities: a) demutualisation b) rematerialisation, c) electronic shares d) dematerialsation,

107. The term 'Green-shoe option' is used in relation to:- a) environment audit, b) 2d green revolution, c) capital mobilized by plantation companies d) option to retain that portion of the equity that has been subscribed by the public over and above the issued amount e) option to return the amount of capital that has been received in excess of the issued amount

108. Which of the following instruments represent the share in Indian companies in India being traded in America/Europe? a) GDR/ADR, b) IDR/ADR, c) GDR/IDR, d) Zero Coupon Bonds Debentures

109. The stock-index futures contracts are the contracts relating to:- a) stocks of commodities b) stocks of industrial products stocks/shares being traded at stock exchanges, c) stocks of d) infotech companies

110) ESOP stands for:- a) efficient servicing of promises, b) employees' service option projects, c) employees stock option plan, d) effective system of projects

111) The term CBLO in connection with short term market related borrowing, stands for:- a) collateralized banking and lenders' obligation, b) common borrowing and lending obligation c) collateralized borrowing and lending obligation d) collateralized borrowing and lending organization

112) The demat shares of a public sector undertaking can be converted in to physical shares. This process is called:- a) re-issue of shares, b) dematerialisation of shares c) re-materialisation of shares d) demutualisation of shares, e) forfeiture of shares

113) Interest rate on a debt security (say Govt. bonds) which issuer pays to holder till maturity:-

a) interest, b) yield, c) floating rate, d) coupon rate

114) When buying or selling of securities is done by a person having access to privileged information, it is known as? a) Secular trading, b) Insider trading, c) Over trading, d) Unauthorized trading, e) Any of the above

115) The term 'round tripping' in case of Foreign Direct investment relates to: a) coming back of domestic money as FDI b) use of FDI funds out of country, c) sending back foreign money as export, d) a and c above.

116) In order to obtain cash for its credit sales, the duly accepted domestic sale invoices are assigned by the seller in favour of a 3rdparty. Such purchase of receivables by the 3rd party with or without recourse is called: a securitization, b factoring, c bills discounting, d forfeiting, e any of above

117 Branches of banks distribute to their customers as corporate agents, insurance products of other insurance companies, which is called:

a underwriting business, b bancassurance, c referral business, dany of the above

118 Ais a contract where the purchaser of the option has the right but not the obligati on to either purchase or sell and the seller of the option agrees to sell or purchase an agreed amount of a specified currency at a price agreed in advance and denominated in another currency :
a interest rate swap, b forward rate agreement, c currency option, dforeign exchange forward

119 When a company instead of fixing the price of new share, invites bids and allows the market to fix the price of the share, the process is called:
a private placement, b price search, c book-building, d initial public Offering, e market price fixation

120 The temporary loans that are allowed by RBI to Govt. from time to time to meet the mismatch position are called: a) treasury bills
b dated securities, b ways and means advances, c) ad hoc treasury bills

121 In the capital market, the term *arbitrage* is used with reference to which of the following?
A Purchase of securities to cover the sale, B Sale of securities to reduce the loss on purchase, c Simultaneous purchase and sale of securities to make profits from price variation in different markets, d Any of the above

122 The contract notes that are issued by Foreign Institutional Investors (FIIs) to their clients (not registered with SEBI), investing in Indian stock market:
a depository receipt, b derivative, c option, .d participatory notes

123 A is a type of transferable financial instrument traded on a local stock exchange of a country but represents a security issued by a foreign publicly listed company:
a depository receipt, b derivative, coption, d participatory notes

124 All the sales practically become cash sale to the seller in respect of :
a Leasing, b Acceptance credit, c Factoring, d Buyer's credit

125 In order to obtain cash for its credit sales, the duly accepted domestic sale invoices are assigned by the seller in favour of a 3rd
party. Such purchase of receivables by the said 3rd party with or without recourse is called:
a securitization, b factoring, c bills discounting, d forfeiting

126 Which of the following methods can be conveniently used for providing finance to infrastructure projects:
a securitization, b factoring, c credit syndication, d consortium financing, e take out financing

127 Narrow money is the term in monetary aggegates which is represented by:- a M1 b M2, c M3 d M4

128 In banking, the banks offer all types of financial services to expand their business that include high risk products and medium risk products also:- a retail banking, b universal banking, c wholesale banking, d narrow banking

129 When an existing non-profit organisation is converted into a for-profit company, the process is called :
a Dematerialization, b Demutualization, c Re-materialization, d Re-rnutualization

130 A is a financial contract between two parties to exchange interest payments for a 'notional principal' amount on settlement date, for a specified period from start date to maturity date. a) nterest rate swap, b) forward rate agreement, c) interest rate future, d) foreign exchange forward.

131.What is meant by the term reverse REPO out of the following:
a) injecting liquidity by the Central Bank of a country through purchase of govt. securities, b) absorption of liquidity from the market by sale of govt. securities, c) Balancing liquidity with a view to enhance economic growth rate, d) Improving the position of availability of the securities in the market.

132 A is a financial contract between two parties exchanging or swapping a stream of interest payments for a `notional principal' amount on multiple occasions during a specified period.
a interest rate swap, bforward rate agreement, c interest rate future, d foreign exchange forward

133 Transformation of certain processes and procedures with a view to empower the bank with

contemporary technologies, business solutions and innovations that enhances the competitive advantages is called:
a business process modifications, b business process re-engineering, cbest practices code, dbusiness re-modeling
134 A - is an over-the- counter contract under which a purchaser agrees to buy from the seller, and the seller agrees to sell to the purchaser, a specified amount of a specified currency on a specified date in the future at a known price denominated in another currency:
a) interest rate swap, b) forward rate agreement c) interest rate future, d) foreign exchange forward
135. When an unlisted company issues fresh securities for the first time, it is called: a) initial public offering, b) rights issue, c) follow-on public offering d) bonus shares
136. A negotiable security issued outside India by a Depository bank, on behalf of an Indian company, which represents the local Rupee denominated equity shares of the company held as deposit by a Custodian bank in India, is called : a) Derivative, b) Depository receipt, c) FDI, d) Indian Depository receipt.
137. The depository receipts listed and traded in the US markets are known as :- a) Global Depository Receipts b) Indian Depository Receipts, c) American Depository Receipts, d) Derivative Instruments A
138. bond giving the investor the option to get the value of bond equal to an equity share, at a pre-determined exchange price, is called: a) coupon bonds, b) convertible bonds c) commercial paper d) zero coupon bonds
139. The depository receipts listed and traded anywhere/elsewhere other than in United States, are known as:- a) Global Depository Receipts b) Indian Depository Receipts c) American Depository Receipts, d) Foreign Currency convertible bond
140. In which of the following kinds of financing the banks can take up financing for medium term (5-7 years) out of the very long term nature of the projects (1520 years):- a) Securitization, b) Take out financing, c) Project participation d) Consortium
141. Process of artificially increasing or decreasing prices of a security:- a) insider trading, b) circular trading, c) price rigging, d) any of the above
142. Interest spread refers to: a) surplus of interest earned over interest expended b) interest earned on loans less the provisions
d) interest earned on loans and investments less provision e) none of the above
143. The market based approach aimed at neutralizing part or whole of• the monetary impact of foreign exchange inflows is termed: a) sterilization, b) neutralization, c) globalization, d) liquidity adjustment
144. The term broad money is known as:- a) M1 b) M2, c) M3 d) M4
145. What is an American Depository Receipt? a) An instrument denominated in US dollars, b) An instrument issued to non-resident c) investors, aaainst ordinary shares, d) An instrument fulfilling the features given in A and B, d A or B
146. There are certain financial instruments whose prices are derived from the price of the underlying currency or interest rate or stocks etc. These are known as:- a Securitisation,
b Derivatives, C Leasing, d Factoring e Venture Capital Funding
147 Which of the following is not an instrument of derivatives:- a forwards, b options, c futures a to c, e none of these
148 An option that provides to the option holder, a right to sell, without an obligation to sell , is called:
a put option, bcall option, c American option, d European option
149 An option that provides to the option holder, a right to purchase, without an obligation to purchase, is called:
a put option, b call option, c American option, d European option
150 An option that can be exercised any time during its validity period, is called:- a put option, b call option, c American option, d European option
151 An option that can be exercised on a specified day,. during its validity period, is called:-
a put option, b call option, c American option, d European option

152 What is an option ? a a right to sell only without obligation to sell, b a right to purchase only without obligation to purchase, c a right to sell or purchase, d without obligation to sell or purchase, d obligation to purchase or sell without any right to sell or purchase

153 Where exercising the option provides gain to the buyer, it is called
a at the money, b in the money, c out of money, d above the money

154 Where exercising the option results in loss to the buyer, it is called:-
a at the money, b in the money, c out of money d above the money

155 Where exercising an option provides gain or loss to the buyer, it is called
a at the money, b in the money, c out of money d above the money, e) Govt. Securities

156: Gilt-edged market deals in: a: Worn currency notes, b) Bullion and gold, c) Govt. securities, d) Corporate bonds, e) all kinds of capital market securities

157 In respect of investment in securities, the process under which the value of the securities is taken into account at their current market price is called:- a pricing of securities, b marking to market, C valuation of d securities any of the above

158 The securities that are purchased by banks with the intention to take advantage of price movement or interest movement, are classified as:
a held till maturity, b available for sale, c held for trading, d fluctuating securities

159 A govt. security that has been authorised to be issued but has not been issued actually, as yet called:
a gilt-edged security, b approved security, when, as and if issued, d ways and means advance, e treasury bill

160 What is the maturity period of treasury bills issued by Govt. of India:- a 14 and 91 days, b 91 & 182 days, c 14 & 182 days, d 91,182 & 364 days, e) none of the above

161 Ways and means advances of the Central Govt. are payable within a period of?
a 10 days b 18 days, b: 15 days d c) 20 days, d) 14 days

162 The maturity period of a cash management bill can be:- a less than 364 days, b less than 182 days, C less than 91 days, d any period at discretion of the Govt.

163 Under WMA RBI has allow the States to run overdrafts for consecutive working days from Feb 01, 2001 instead of the then 10 Days:- a 09 days b I 1 days, c 14days d 15 days, e Call and Notice Money

164 The market for short term financial assets instruments, that are close substitutes of money, is called:- money market b) capital market c) forex market d) financial market

165. Under market, the funds are transacted by banks on an overnight basis:
a) money market, b) call money market, c) notice money market d) term money market

166. Under notice money market, the funds are transacted by banks for:- a) one day, b) overnight, c) 2 to 14 days d) 15 days and above

167. On a fortnightly average basis, the prudent limit fixed by RBI in respect of outstandingborrowing transactions in call and notice money for the participating banks is:

a) 100% of capital of bank b) 100% of capital + reserves of the bank, c) 100% of capital fund of the bank, d) 100% of net worth of the bank.

168. As per the prudent limit fixed by RBI in respect of outstanding borrowing transactions in call and notice money for the participating banks, the banks can borrow a maximum of on any day, during the fortnight:-
a 110% of their capital fund, b 120% of their capital fund, c 150% of their capital fund, d 125% of their capital fund

169. On a fortnightly average basis, the prudent limit fixed by RBI in respect of outstanding lending transactions in call and notice money for the participating banks is:-
a 10% of capital of bank, b 15% of capital + reserves of the bank, c 25% of capital fund of the

bank, d 30% of net worth of the bank

170 As per the prudent limit fixed by RBI in respect of outstanding lending transactions in call and notice money for the participating banks, the banks can borrow a maximum of on any day, during the fortnight:

a 20% of their capital fund, b 30% of their capital fund, c 50% of their capital fund, d 50% of their net worth

Certificate of deposit and Commercial Paper

171 Which of the following features of certificate of deposit is correct (1) CD is a negotiable market instrument (2) CD is issued in demat form or as a usance promissory note (3) CD is issued at a discount to face value:- a 1 to 3 all, b 1 and 2 only, c 2 and 3 only, d1 and 3 only

172. Which of the following statement regarding amount of certificate of deposit is correct:

a) minimum amount is Rs.1 lac and maximum Rs. I cr b) minimum amount is Rs 1 lac without any maximum but multiple should be of Rs.5 lac, c) minimum amount is Rs.1 lac without any maximum but multiple should be of Rs.2 lac, d) minimum amount is Rs.1 lac without any maximum but multiple should be of Rs.1 lac

173. Certificate of deposit issued by banks can have a maturity period of:- a) 15 days to 12 months, b) 15 days to 6 months, c) 15 days to 3 months, d) 7 days to 12 months

174. Which of the following statement regarding certificate of deposit is correct (1) banks can grant loan on security of CD (2) banks can buy back the CDs before maturity (3) CD can be freely transferred any time after issue (4) CRR and SLR is applicable on CD:- a) I to 4 all, b) 2 and 4 only, c) 3 and 4 only, d) 1 and 4 only

175. Commercial Paper (CP) is an unsecured money market instrument issued in the form of:- a) a debenture certificate, b) a share certificate, c) a usance promissory note, d) a bill of exchange.

176. For a company to issue commercial paper which of the following conditions to be fulfilled are correctly stated (1) the net worth should be at least Rs.4 cr (2) the company should have been sanctioned working capital limits of Rs.10 cr (3) the loan accounts the company should be classified as Standard loan by its banks (4) it should have a credit rating of at least A3 by an approved credit rating agency.:- a 1 to 4 all, b 1,2 and 4, c I, 3 and 4, d 1 to 3

178. The maturity period of Commercial paper falls within the following range:- a 7 days to 3 months, b 7 days to 6 months, c7 days to 9 months, d 7 days to 12 months

179. The minimum amount of and multiple of commercial paper should be:- a Rs.1 lac, Rs.1 lac, b Rs.1 lac, Rs.5 lac, c Rs.5 lac, Rs.5 lac, d Rs.5 lac and no multiple.

Credit Card Operations

180. The term plastic money relates to which of the following:- a credit card, b prepaid phone card, c plastic sheet notes, d all the above

180 Credit card business can be conducted by banks only if their net worth is at least Rs.

a Rs.100 cr, b Rs.200 cr, c Rs .300 cr, d Rs.500 cr

181 In case of credit card, the customers can lodge a complaint with the banks within a period of :

a 15 days, b 30 days, c 45 days, d 60 days

182 Revolving credit is made available in which of the following:- a a debit card, b a pre-paid card, C a credit card, d all the above

183. In case of a credit card, if a customer protests any bill, the bank should provide explanation or documentary evidence withina maximum period of days to amicably redress the grievances.

a 10 days, b 15 days, c 30 days, d 60 days

184. In case of a credit card if a complainant does not get satisfactory response from the bank within a maximum period of days from the date of his lodging the complaint, he will have the option to approach the Office of the concerned Banking Ombudsman for redressal of his grievance/s.

a 10 days b 15 days, c 30 days d 60 days

185. In case of acard, the customer can make payment to the extent of balance lying in his account.

a debit card, b smart card, c credit card, d any of the above

Inter-Bank Liabilities

186 In case of bank having higher CRAR of 25% over the regulatory CRAR of 9%, the maximum amount of inter-bank liabilities of a bank can be of net worth of the bank as on March 31 of the previous year:

a 100% , b 150%, c 200%, d 300%

187 The maximum amount of inter-bank liabilities of a bank can be of net worth of the bank as on March 31 of the previous year:

a 100% b 150%, c 200% d 300% e Marginal Standing Facility

188 What is the amount for which the marginal standing facility (MSF) can be availed by banks from RBI:

a minimum Rs. 1 cr and multiple of Rs.50 lac, b minimum Rs 1 cr and multiple of Rs.1 cr, c minimum Rs.5 or and multiple of Rs.1 cr, d minimum Rs.5 cr and multiple of Rs.5 cr

189 Under the marginal standing facility (MSF), the eligible entities can avail the facility, up to per cent of their respective Net Demand and Time Liabilities (NDTL) outstanding at the end of the second preceding a) 3% b) 1% c) 2%, d) 0.5%

190. Under the marginal standing facility, what is the time period for which the facility can be generally availed from RBI:

a) 10 days and 12 days on Friday, b) 7 days and 9 days on Friday, c 1 day and 3 days on Friday, d RBI discretion

FDI in Banks

191. What is the maximum ceiling on Foreign Direct Investment (FDI) for investment in the equity of private banks in India:

25% b 26%, c 49% d 51%, e 74%

192. What is the maximum ceiling on Foreign Direct Investment (FDI) for investment in the equity of public sector banks in India:

20% b26%, c 49% d 51%, e 74%

193. An infrastructure finance company can deploy _% of its total assets in infrastructure loans:

50%_ b51%, c 74%d 75%

194. Under takeout financing (refinancing) of project loans, the banks can takeover the standard loan from other banks; provided the aggregate exposure of all institutional lenders to such project should be minimum:- a) Rs. Rs.100 cr b) Rs.250 cr c) Rs.500 cr d) Rs.1000 cr

195. RBI treats Core Investment Companies having an asset size of as systemically important core investment companies:- a) Rs.10 crore and above b) Rs.50 crore and above c) Rs.100 crore and above d) Rs.200 crore and above

196. A non-banking financial company which carries on the business of acquisition of shares and securities and satisfies certain conditions, is called:- a) Investment company b) financial company, c) non-bank finance company d) core investment company

197. Core investment companies will be treated as systemically important core investment company, if its assets size is a) Rs. Rs.50 cr and above, b) Rs.100 cr and above, c) Rs.200 cr and above, d) Rs.500 cr and above

198. A core investment company must hold not less than of its net assets in the form of investment in equity shares, preference shares, bonds, debentures, debt or loans in group companies

a) 100% b) 90%, c) 74% d) 60% SEBI Rules

199. The time gap between closure date of a public issue and its listing on stock exchange, has been reduced by SEBI from to

a) 42 days to 30 days b) 30 days to 22 days, c) 22 days to 12 days d) 30 days to 15 days

200. Listed companies are required to disclose their quarterly financial results within from close of the quarter:

a) 15 days b) 30 days, c) 45 days **d)** 60 days

201. Listed companies are required to disclose their annual audited results within from close of the financial year:

a 15 days b 30 days, c 45 days d 60 days

202 As per SEBI directives, what is the minimum public shareholding in case of listed companies:
a 10% b 24%, c 25% d 26%, e 49%

Misc. Questions

203 Under which kind of following mechanisms, the D SB returns being submitted by banks to RBI, fall:
a early alert system, b on-site surveillance, c off-site supervision, d risk based supervision system e prevention of money laundering

204 Negotiated Dealing System relates to:- a trading at stock markets, b Settlement of security dealings
c trading in Govt. securities, d Settlement of share payments, e aandb

205 Which of the following extension of abbreviation does not match:
a BCSBI — Banking Codes and Standards Board of India, b BCBS — Banking Codes and Banking Standards
c BFS — Board for Financial supervision, d BIFR — Board for Industrial and Financial Reconstruction

206 Banks are required to ensure that while preparing their Annual Branch Expansion Plan (ABEP), they should allocate at least of the total number of branches proposed to be opened during a year in unbanked rural (Tier 5 and Tier 6) centres.
20% b 25%, c 33% d 40%

207. To promote a joint venture or a subsidiary for with risk insurance business of underwriting, the minimum net worth of the bank should be: a) Rs.200 cr, b) Rs.500 cr, c) Rs.1000 cr, d) Rs.2000 cr

208. Operating profits in bank's profit and loss ° account refer to:
a) net profits, b) profits before contingencies c) profits before provisions and contingencies, d) profits after provisions and contingencies

209. For banks to enter into insurance sector for underwriting with-risk business, among others, the CRAR should not be less than:- a) 8% b 9%, c) 10% d 11%, e) 12%

210. As per Exchange Traded Currency Options (RBI) Directions 2010, the underlying for the currency option shall bespot rate;
a) Euro-Indian Rupee spot rate b) USD-Indian Rupee spot rate, c) USD & Euro -Indian Rupee spot rate, d) Pound -Indian Rupee spot rate

211. To promote a joint venture or a subsidiary for with risk insurance business of underwriting, the minimum net worth of the bank should be:- a Rs.200 cr, b Rs.500 cr, c Rs.1000 cr, d Rs.2000 cr

212 The term TReDS, in the context of financing of working capital of MSME, means:
a TradeReceivables Discounting System, b Time Receivables Discounting System, c Trade Related Discounting System, d Trade Receivables Distribution System

213 Under the rating system called CAMELS, the term `M' stands for which of the following:
a management of assets and liabilities, b management of nonperforming assets c management of human resources
d management effectiveness, e management policies

214 The letter C in the rating model CAMELS being used by RBI for rating Public Sector Banks represents:
a Capital fund, b Capital adequacy, c Capital contributed to subsidiaries, d b & c

215 RBI's Model for Rating of Indian Banks is known as:- a CAMELS, b CAMEL,
c RATING, d e-CAMEL

216 What is Net Interest Income (Nu)? a Difference of interest, earned on assets and non-interest income, b Difference of assets and liabilities, c Difference of interest earned on assets and interest paid on liabilities, d None of the above.

217 What is RBI's objective in asking banks to move from quarterly to monthly system of interest charging ?
A as part of 90 days norms for identification of non- performing advances, B introduction of international standard

C early recovery of interest to increase income of banks, d introduction of simple interest rates

218 What is true with regard to payment of dividend by a commercial bank:

a maximum dividend that can be paid is 33.33%, b maximum dividend payment is 25%, c maximum dividend that can be paid is 40%, d maximum dividend payout ratio is 40%, e there is no restriction on dividend payment if bank is in profit and CAR is 9%

219 Non-Convertible Debentures may be issued in denominations with a minimum of (face value) and in multiples of

A Rs.l lac, Rs.1 lac, b Rs.5 lac. Rs.1 lac, c Rs.5 lac, Rs.5 lac, d Rs.5 lac, Rs.10 lac

220 Which of the following terms represent 'one basis point':

a one percent, b one tenth of one percent, c one hundredth of a percent, d one hundred percent, e one thousandth of a percent

221 Bombay stock exchange index `Sensex' is based on the value of top blue chip shares of:

a 10 b 20, c 25 d 30, e 50

222 Which of the following category of securities are not required to be marked to market by banks:

a held till maturity, b available for sale, c held for trading, d none of the above

223 The held for trading securities are required to be sold within

a 360 days, b 180 days, c 90 days, d there is no such time constraint.

224 All credit institutions are required to become members of a credit information company under provisions of Credit Information Companies (Regulation) Act 2005. A bank can become member of which of the following:-

A Credit Information Bureau (India) Limited, b Experian Credit Information Company of India Pvt Ltd, c Equifax Credit Information Services Pvt Ltd, d any of these

225 The credit institutions are required to update the credit information on a regular basis at least on basis, to provide the information to Credit Information Companies:

a) Monthly, b) quarterly, c) Half-yearly, d) Yearly

226. The SLR and non-SLR securities of the banks are classified into 3 categories. Which of these is not part of those 3 categories:- a) held till maturity b) available for sale c) held for trading d) none of the above

227. RBI changes the CRR. Which of the following is correct in this connection:- a) reduction in CRR increases the liquidity position within Indian banks, b) increase in CRR increases the liquidity position within Indian banks, c) increase in CRR does not affect the liquidity position, d) decrease in CRR does not affect the liquidity position

228. When Repo rate is reduced by RBI, it leads to :- a)_ reduction of cost to borrowers on bank loans, b) increase in cost of loans to borrowers from banks, c) reduced cost of borrowing by banks from RBI d) increased cost of borrowing by banks from RBI

229. When RBI offers liquidity adjustment facility to banks this leads to (a) improvement in the liquidity position of banks (b) increase in their capacity to lend (c) increase in their deposits (d) improvement in income of banks by more lending a) a to d all, b) b and c, c) b and d, d) c and d

230. What is the objective of securitisation of financial assets?

a) to enable the banks in speedy recovery of bad loans, b) to sell the securities without intervention of the court, only if loan gots bad c) to acquire assets and then sell the same at profit, d) recycling of funds and reduce concentration risk e) a to d all

231. The minimum paid-up equity capital for small finance banks shall be Rs. crore.

a) Rs.100 cr, b) Rs.200 cr c) Rs.300 cr d) Rs.500 cr

232. As per 5E131 guidelines, the mandatory minimum shares buy-back has been increased to % of the amount earmarked for the buy-back, as against existing %,

a) 25% from 10% b) 35% from 25% c) 50% from 25% d) 50% from 30%

233. As per SEBI guidelines, the maximum shares buy-back period has been reduced to months from months. a) 6 months to 3 months b) 9 months to 6 months c) 12 months to 6 months d) 12 months to 9 months.

234. Minimum paid up capital shall be Rs crore to set up and operate TReDS:

a Rs.10 cr, b Rs.25 cr, c Rs.50 cr

235 Payment Banks are allowed to accept which of the following type of deposits:

a recurring deposits, b fixed deposits, c demand deposits, d all the above Rs.100 cr

236 The small finance banks will extend per cent of its Adjusted Net Bank Credit to the sectors eligible for classification as priority sector lending by RBI. a 3 2 % b 4 0 % , c 6 0 % d 7 5 %

237 At least 50% of loan portfolio of a Small Financing Bank should constitute loans and advances of upto Rs. lakh. a Rs. 5 lac, b Rs.10 lac, c Rs.25 lac, d Rs.50 lac

238 Payments Bankswill initially be restricted to holding a maximum balance of Rs. Per individual customer.

a Rs.10000, b Rs.50000, c Rs.100000, d Rs.200000

239 Apart from amounts maintained as Cash Reserve Ratio with the Reserve Bank on its outside demand and time liabilities, a Payment Bank\ will be required to invest minimum per cent of its "demand deposit balances" in Statutory Liquidity Ratio eligible Government securities/treasury bills with maturity up to one year. 25%b 50%, 60% d 75%

240. The minimum paid-up equity capital for Payments Banks shall be Rs. crore.

a) Rs.100 cr b) Rs.200 cr, c) Rs.300 cr d) Rs.500 cr

ANSWER

1	C	2	B	3	A	4	B	5	C	6	B	7	C	8	C	9	D	10	D
11	B	12	D	13	D	14	A	15	B	16	D	17	C	18	D	19	A	20	A
21	A	22	A	23	A	24	B	25	A	26	D	27	C	28	C	29	D	30	B
31	B	32	C	33	C	34	D	35	D	36	C	37	C	38	D	39	B	40	B
41	B	42	C	43	C	44	D	45	B	46	B	47	A	48	B	49	D	50	D
51	A	52	C	53	C	54	D	55	B	56	D	57	A	58	C	59	B	60	D
61	D	62	A	63	A	64	C	65	D	66	A	67	C	68	D	69	A	70	B
71	A	72	B	73	D	74	C	75	B	76	D	77	C	78	C	79	C	80	A
81	B	82	A	83	B	84	C	85	C	86	E	87	C	88	B	89	D	90	C
91	C	92	A	93	C	94	B	95	C	96	E	97	C	98	A	99	B	100	B
101	C	102	C	103	C	104	B	105	C	106	D	107	D	108	A	109	C	110	C
111	C	112	C	113	D	114	B	115	B	116	B	117	B	118	C	119	C	120	C
121	C	122	D	123	A	124	C	125	B	126	E	127	A	128	B	129	B	130	B
131	B	132	A	133	B	134	D	135	A	136	B	137	C	138	B	139	A	140	B
142	A	143	A	144	C	145	C	156	B	147	E	148	A	149	B	150	C	151	D
152	B	153	C	154	C	155	A	156	C	157	B	158	C	159	C	160	D	161	A
162	C	163	C	164	A	165	B	166	C	167	C	168	D	169	C	170	C	171	A
172	D	173	D	174	C	175	C	176	C	177	D	178	C	179	A	180	A	181	D
182	C	183	D	184	C	185	B	186	D	187	C	188	B	189	B	190	C	191	E
192	A	193	D	194	D	195	C	196	D	197	B	198	B	199	C	200	C	201	D
202	C	203	C	204	C	205	B	206	B	207	C	208	C	209	C	210	B	211	C
212	A	213	D	214	B	215	A	216	A	217	A	218	D	219	B	220	E	221	D
222	A	223	C	224	D	225	A	226	D	227	A	228	C	229	C	230	D	231	A
232	C	233	C	234	B	235	C	236	D	237	C	238	C	239	D	240	A		

TEST YOUR SELF

PRACTICE TEST PAPERS

(BASED ON IIBF TEST PATTERN)

ADVANCED BANK MANAGEMENT

(CAIIB PAPER -1)

PRACTICE TEST PAPER NO. A (TEST YOUR SELF)

QUESTIONS BASED ON MEMORY

1) Net Interest income is: a)Interest earned on loans and advances only b)Interest earned on investments only c)Total interest earned on advances and investment d)Difference between interest earned and interest paid

2) Investment made by a bank in its subsidiary is considered in the following category in its balance sheet:
a) Secured advances b)Other assets c)Investments d) Unsecured advances

3) Net Interest Income (NII) is calculated using the following formula : a) Interest income - Total expenses b)Total income - Interest expenses c)Interest income - Interest expenses d) Total income - Total expenses

4) N.I.M. calculated using the following formula:a) Nil /Average total liabilities b)NII /Average Total Assets c)Total Interest Income /Average Total Assets d)Total interest Income /Average Total Liability

5) Economic Equity Ratio is used to assess sustenance capacity of the,bank• It is calculated using the formula:
a) Net Interest Income / Shareholder Funds b)Total Income / Shareholder Funds
c)Shareholder Funds Total of Assets & Liabilities d)Shareholder Funds Total Assets

6) Risk of having to compensate for non-receipt of expected cash flows by a bank is called:
a) Call risk b)Funding risk c)Time risk d) Credit risk

7) 'Time risk' in the context of liquidity risk of an institution is caused due to:
a) Systematic risk b)Swaps and options c)Loss of confidence d) Temporary problems in recovery

8) Crystallisation of contingent liabilities in a bank is called: a) Call risk b)Funding risk c)Time risk d) Credit risk

9) If the volatility per annum is 25% and the number of trading days per annum is 252, find the volatility per day.: a) 58% b)1.60% c)158% d) 15.8%

10)RBI has put in place real time gross settlement system (RIGS) to mitigate the following risk:
a)Markel risk b)Settlement risk c)Operational risk d) Strategic risk

11) A bank is having Rs 500 Crore liabilities @ 7% of one year maturity to fund Rs 500 Crore assets @ 9% with 2 year maturity. The bank is exposed to: a) Gap Risk b)Basis Risk c)Price Risk d) Yield Curve Risk

12) In India, type of options are permitted now: a) American b)European c)Asian d) A & B

13) Interest rate risk is a type of :a) Credit risk b)Market risk c)Operational risk d) All the above

14) If Regulatory Authority of the country feels that the Capital held by a bank is not sufficient, it could require the bank to: a) Reduce it's Risk b)Increase its Capital c)Both of these d) Either of these

15) When a bank sanctions a loan to a large borrower, which of the following risks it may not face:
a) Liquidity b)Market c)Credit d) Operational

16) A firm has an opening of stock of Rs.70,000. Closing stock of Rs.90,000 and Cost of goods sold Rs.2,40,000. What the Inventory Turnover Ratio? a)5 b)4 c)3 d) 2

17-18) Based on the following information, solve questions number 17&18.

Credit Sales - Rs.3,00.000
Opening Balance of Accounts Receivable - Rs 40,000
Closing Balance of Accounts Receivable - Rs.60,000
Credit Purchases - Rs.1,80,000
Opening Balance of Account Payable - Rs 20,000
Closing Balance of Accounts Payable - Rs.40.000

17) The Debtors' Turnover Rati6 is: a) 6 b)8 c)10 d) 12

18) The Creditors' Turnover Ratio is: a) 8 b)6 c)4 d) 2

19) To solve a standard maximization problem using the Simplex method,we take the steps which are jumbled. Mark the correct order of steps.
Step 1: Determine which variable to bring into solution Step 2: Determine which variable to replace
Step 3: Formulate problem in terms of an objective function and a set of constraints
Step 4: Update remaining Row values Compute new z
Step 5: Calculate new row values for entering variable and insert into new tableau.
Step 6: Set up initial Tableau with slack variables
Step 7: If there is no positive (c-z) value found, the solution is optimum. If there is a positive value, then iterate again (repeal earlier three steps)
Choose the correct sequence of steps.: a) 3,5,4,5.7,1,2 b)3,6,2,1,5,4,7 c)3,6,2,1,4,5,7 d) 3,6,1,2,5,4,7

20) Which of the following is not a motive for the companies to hold cash?: a) Transaction motive b)Precautionary motive c)Lack of proper synchronizationbetween cash inflows & outflows d)Capital Investments

21) VaR means:a) Volume of Business at Risk b)Value at Risk c)Volume on Risk d) Value as Risk

22) The maximum loan against NRE/FCNR Term deposit was Rs.20 lakh earlier. RBI has now increased it to:
a) Rs.25 lakh b)Rs. 1 crore c)Rs.50 lakh d) No change
23) Credit Risk Assessment of the borrowal units is for: a) Assessing the repayment capacity b)To fix the pcing of the product c)To review the units performance d) None of the above
24) Pricing is equals to :a) Cost of the product b)Break Even Point of the firm
c)Function of Risk rating d) All of the above
25) The bond prices can be estimated using modified duration. The formula for calculating %age change in price of a bond is: a)Modified duration x yield change b)Yield change /modified duration
c)Modified duration 1 Yield change d)Modified duration + Yield change
26) If both the Regression coefficients are negative, the correlationcoefficient would be :
a) Positive b)Negative c)Zero d) None
27) The most frequently used Average is: a) Mode b)Median c)Mean d) Geometric Mean
28) Advance in the form of Pledge cannot be granted in respect of
a) Stock-in-process b)Raw material c)Finished goods d) Stores
29) In which of the following methods of capital budgeting annual returns of the future years are discounted to their present value : a) Pay back period b)Internal rate of return c)Present value method d) Both 'a' & 'c'
30) Bonds may be secured by :a) Floating charge on assets b)Fixed charge on assets c)Without charge d) All of these
31) Which of the following statement is correct? :a)Forex markets are localized markets b)Forex markets are International markets only c)Forex markets are dynamic & round the clock markets d)Forex markets are used only for trade transactions
32) If market quotes USD(INR as 53.61/63,at what rate can you buy USD at the given quote?:
a) 53 61 b)53 62 c)53 33 d)53 61
33) The main role function of the Welfare secretary was to meet the needs of the workers and prevent them from .:
a) Forming Unions b)Leaving the job c)Gossiping during duty d) Disturbing other workers
34) Union formations were seen in the_____phase of development of HRM:
a) First phase b)Second Phase c)Third phase d) Unions have been present even before HRM came in to existence
35) Climate Management is possible by using HRIT. Climate information is gathered using: a)Job satisfaction surveys b)Performance appraisals by superiors c)Studying attendance patterns in different weathers d)AIL of the above
36) Job Analysis technique involves: a) Job Description b)Job Specification c)Job Evaluation d) All of the above
37) Mechanistic (or Behaviorist) theories, Cognitive theories and Organismic (humanistic)theories are three theories of learning. Which one of these theories equates man with his brain?
a) Behaviorist or mechanistic theories b)Cognitive theories c)Organismic or humanistic theories d) All of the above
38) The Concept of Career path relates to of movements and deciding the_____for each stage.:
a) Sequence, time period b)Number, candidates c)Decision, number d) Type, time period
39) Johari Window is most useful for:
a) Understanding others b)Self-Awareness c)Working in Teams d) Improving inter-personal relations
40) The process of capturing the tacit knowledge of people in a systematic manner for future use is called:
a) Data entry b)Information technology c)Knowledge management d) All of the above together
41) Mandatory feature of a Letter of Credit: a)Must have an applicant and a beneficiary b)Should have an advising bank and a confirming bank c)Should be confirmed to be operative d)Must be confirmed by the reimbursing bank
42-45)The top management of ABC Bank was in a triumphant mood after engaging XYZ Ltd, one of the top IT Companies as a consultant for a massive technology upgradation in the Bank. Their enthusiasm was short lived, as the project did not progress well and the consultants were not able to deliver the desired results even after several months. In fact the Consultants were of the view that it may never be possible to implement the project with 100% success as they seemed to be facing resistance from the employees at multi-levels. The employees at all levels seemed reluctant to co-operate. Their fear of Role erosion seemed palpable.
42) What does "Role erosion" mean in this context?: a)The fear of the employee that he will be sent out b)Fear that the responsibility and the power will reduce c)Fear that he will no more be an indispensable d) a & b
43) The critical issue in this case is:
a)Attitudes of individuals b)Training of people c)Group behavior due to a sense of the unknown d)All the above
44) How could this situation have been managed better?: a)By issuing project details and time frame mentioning punishments in case of delay b)By roping in the HR professionals to act as coordinator c)By recognizing that any change brings its own reactions and co-opting the managers even before the Consultants moved in d)b & c
45) The Bank should deal with the employee resistance by: a)Co-opting the employees b)Communicating strategically about the potential benefits c)Conducting simultaneous training to familiarize the staff with the new software d)All of the above
46) Mr. Ganguli is a brilliant manager in ABC Bank. He is one of the few persons picked up by the top management from an IIM after MBA. Always on two phones at a time, he boasts about having no patience with tt laggards. Often, he can be heard aggressively yelling at people on small issues. What type of person is Mr. Ganguli?:
a)Type B personality b)Type A personality c)Type C person d) Type D person

47) What is most essential for achieving Work-Life balance?:
a) Time management b)Efficiency c)Assertiveness d) Emotional maturity
48) A sales man in a shop showed a suit piece and told the customer that the cloth is very good, but costly. He was using the following transaction: a) Duplex b)Angular c)Complementary d) None of the above
49) A prominent politician was heard saying that that people state was incapable of joining the army. He was :a)Stereotyping b)Projecting c)Hallucinating d) All of the above
50) Mr. A is the Branch Manager in ABC Bank. He makes it a point to visit the prominent deposit customers himself to deliver their deposit receipts. He does not even take the "Relationship Manager" appointed for this purpose. Mr. A believes that none of the new generation staff is good enough to deal with such tasks. What is the "Life position" taken by Mr. A as regards the "Relationship Manager" as per the "Theory of Lifr position" propounded by Dr. Thomas Harris?: a) I are OK, you are OK b)I am Ok, You are not OK c)I am not OK, you are not Ok d) I am not OK, you are not OK
51) Translation losses are significant for banks as they affect the Bank's: a) Markel value b)Interest income c)Both (a) & (b)above d) All of the above

ANSWER

1	D	2	C	3	C	4	B	5	D
6	C	7	D	8	A	9	A	10	B
11	A	12	D	13	B	14	C	15	B
16	C	17	A	18	B	19	D	20	D
21	B	22	B	23	B	24	C	25	A
26	B	27	C	28	A	29	0	30	D
31	C	32	C	33	A	34	A	35	A
36	D	37	B	38	A	39	B	40	C
41	A	42	D	43	C	44	D	45	0
46	A	47	D	48	B	49	A	50-B	51-A

PRACTICE TEST PAPER NO. B (TEST YOUR SELF)

BASED ON RECOLLECTED QUESTIONS

1) As per RBI guidelines, Banks have to report their business, for public reporting purposes, based on segments, segments as and :a) Locational; Domestic; Global b)Market; Domestic , International c)Price; Dollars; Euro. d) Value; Quantitative; Qualitative.e) Geographical; Domestic, International
2) As per RBI guidelines, banks have adopted the business segments, for public reporting purposes:
a) Treasury b)Corporate! Wholesale Banking c)Retail banking d) Other Banking Business e) All of the above
3)is used for the purpose of segment reporting which includes the entire investment portfolio.:
a) Treasury b)Retail banking c)Wholesale banking d) Corporate banking
4) The Retail Banking would include exposures which fulfill the following four criteria:
a)Orientation b)Product, c)Granularity d)Low value of individual exposures. e) All of the above
5) BCBS stands for: a) Basel committee on banking supervision b)Blue cross blue shield
c)Basel centre on banking supervision d) None of these
6) What type of information is given by the financial statements of Auditor's report'? ': a) Diversion of funds b)Financial health c)Realization of debts d) Profitability e) All of the above
7) Orientation Criterion is an exposure to the_ :a) Group of people b)Individuals c)Small business d) Both b&c
8) Annual turnover of the Small business is as per segment reporting: a) More than 80 crore b)Less than 50 crore c)More than 50 crore d) Less than 80 crore
9) Product Criterion is the exposure which takes the form of_____credits: a) Revolving credit b)Lines of credit c)Liquidity credit' d) Both a & b e) All of the above
10) In case of Granularity Criterion, aggregate exposure to one counterpart should not exceed_____ of the overall portfolio:a) .5% b).2% c).10% d) .4% e) None of the above
11) Aggregate exposure means__of all forms of debt exposures: a)Net amountb)Gross amount c)Balance d) Net loss
12) Corporate Banking includes advances to thefirms: a) Partnership firms b)Trusts c)Companies d) Statutory bodies e) All of the above
13) Which factors affect the probable consequences likely if a risk does occur:
a) Risk cost b)Risk timing c)Risk scope d) Risk resources e) Both b & c
14) The exposure of a bank to a single NBFC-AFC should not exceed_____percentage:

a) 20-25% b)15-20% c)10-15% d) 5-10%

15) What is the exemption limit for all MSME for obtaining collateral security?
a) Rs 2 lakh b)Rs 5 lakh c)Rs.10 lakh d) Rs15 lakh

16) How much percentages of core assets are required in case of Third Method of Lending as proposed by Tandon committee: a) 100% b)50% c)200% d) 80%

17) ABC analysis divides on-hand inventory into three classet, generally based upon:a) Item quality b)Unit price c)The number of units on hand d) Annual demand e) Annual dollar volume

18) What are the objectives of Credit Audit? a) Improvement in the quality of credit portfolio b))Review sanction process and compliance status of large loans c)Feedback on regulatory compliance d)Independent review of Credit Risk Assessment e) All of the above

19) What are the methods of Return on Investment?:a) NPV b)IRR payback period c)Cost benefit ratio d) Accounting rate of return e) All of the above

20) A project with a high Break-even point is considered_____risky compared to the one with lower break-even point: a) Less b)More c)Equal d) None of the above

21) is the difference between gross fiscal deficit and net lending:
a) Gross fiscal deficit b)Net fiscal deficit c)Net primary deficit d) Revenue deficit

22) Which of the lending arrangement is called Consortium?:
a)When two or more banks get into a formal arrangement to finance the working capital needs of a borrower b)When two or more banks get into a informal arrangement to finance the working capital needs of a borrower.c)When two or more banks get into a informal arrangement to finance the basic needs of a borrower d) None of the above

23) Credit Default Swaps is a bilateral contract in which the risk seller pays a____to the buyer for protection against credit default. a) Discount b)Premium c)Par d) None of the above

24) CDS is a standardized instruments of : a) Credit linked notes b)International Swaps & Derivatives Association c)Internal Swaps and Derivatives Association d) Credit default swaps

25) As per RBI guidelines, only____CDSs are allowed:a) Double vanilla b)Plain vanilla c)Both d) None of the above

26) Stressed assets include which of the following:a) Exit from the accounts b)Rescheduling/Restructuring c)Rehabilitation d) Compromise e) All of the above

27) Which of the following is a tool available to the bank for credit monitoring: a) Analysis of financial statements b)Examine conduct of borrower a/c c)Periodic visits to the business place for inspection d) All of the above

28) What Is the main purpose of Stock audit? : a) To cross check the reliability of the statements b)To examine adequacy of documentation c)To reduce the liquidity d) To increase the turnover e) All of the above

29) Which of the following is the guidelines of RBI for discounting Rediscounting of bills by bank: a)Bank should open LCs and negotiate the bill under LC only b)Bank should mention working capital limit, Bills limit to borrowers after proper appraisal of there credit needs c)Bank should provide credit requirements to the purchaser d)Both a & b

30) Which of the following are non-fund based facilities: a) Negotiate the bills b)Opening of LCs c)Providing Guarantees d) b & c

31) Which of the following aspects covered under economic feasibility of the project: a)Return on investment b)Break even analysis c)Marketing arrangements d) Both a & b

32) The stages of complete Business Cycle are: a)Boom, Recession, Depression, Recovery b)Boom, Depression, Recovery, Recession. c)Peak, Contraction, Trough, Expansion.d) Both a and c.

33) One negative aspect of a Business cycle boom: a)A declining rate of inventory investment. b)A reduction in government budget deficits. c)A declining rate of unemployment d) An increasing rale of inflation

34)is the excess of revenue expenditure over revenue receipts:a) Revenue deficit b)Capital deficit c)Gross fiscal deficit d) None of these

35) The low point in the business cycle is referred to as the:a) Expansion b)Boom c)Depression d)Peak

36)The trough of a business cycle occurs when_____hits its lowest point.:a) Inflation b)The money supply c)Aggregate economic activity d) The unemployment rate

37)The measure of production that values production using current prices is called: a) Underground GDP b) Nominal GDP c) Real GDP d) Value added GDP

38)_____= GDP + Non Resident:a) GNI b)GNP c)GDP d) None of the above

39) C+I+G+(X-M) is the formulae for:a) GNP b)GDP c)GNI d) NR

40)_____ price is the nominal price for which a good or services is offered in the market place:a) Market price b)Economic price c)Marginal price d) Deficit price

41) Which of the following is another derivative of GDP?:a)Income distribution b)Per capita Income c)Human development Index

42) HDI stands for:a) Human democracy Index b)Human development Index c)Higher development Index d) None

43) Which of the following is newest concept of GDP:a) Green GDP b)Blue GDP c)Red GDP d) Yellow GDP

44) The National Income is equal to: a) GNP- Subsidies –Taxes b)NNP-Direct taxes+ Subsides c)NNP- Direct taxes - Subsidies d) GNP- Subsidies +Taxes

45) Which of the following is not true?:a) GNP=Depreciation = NNP b)GNP = GDP + Net income from abroad c)NNPat Factor cost=NNPat Market price + Subsidies - Indirect taxes d)GNP=NNP-Depreciation
46) The difference between GNP and GDP is equal to : a) Gross domestic Investment b)Net foreign Investment c)Net imports d) Net factor income from abroad
47) Net tax revenue + Total non tax revenue = a)Capital receipts b)Total revenuereceipts c)Debt receiptsd) None of these
48) Which of the following items comes under capital expenditure?:a) Defence b)Loan to foreign Governments c)Loan to public enterprises d) All of the above

CASE STUDY - 01

Mr. Mihir is the AGM in charge of Bank street, Hyderabad branch of ABC Bank. He is approached by XYZ Company regarding a TT remittance the Company has to make urgently in favour of Siemens, Singapore for USD One million on Thursday, the 25^0 of Oct. This is the first time the Company is making such a remittance. it is an advance remittance for import of services. The Chairman of XYZ Company is particular that the transaction should go through smoothly. In this regard, please answer the following: •

49) ABC Bank should call for and verify the IIE code of the Company. a) True b)False
50) The exchange rate that would be applicable for this transaction is: a)TT buying b)TT selling c)Bill buying d)Bill selling
51) The Company has to produce a Bank guarantee or Standby Letter of Credit from a First class Bank backing up the remittance because: a)The Advance payment is for a sum exceeding USD 100,000 b)The Advance payment is for a sum exceeding USD 500,000 c)All Advance remittances require BG/SBLC d)BG/SBLC not required any more
52) What is the form that the Company has to submit to the Bank for such an Advance remittance?:
a) Form A-2b)Form A-1 c)Form A-3 d) Form ETX

CASE STUDY - 02

Mr. Mihir, AGM of ABC Bank has arranged for a "Customer Awareness" programme in his branch on 25th Oct. The meeting is attended by customers from all categories such as Exporters, Importers, NRIs etc. A question answer session as follows takes place. Please mark the answers that Mr. Mihir must give in correct response to the customers:

53) Mr. Amrit, CEO of one of the big four auditing firms is a VIP customer residing in Hyderabad. He wishes to know whether he can invest in a residential property in the USA as house prices have become very attractive there now:
a)Yes, he can invest and buy the house. b)No, he cannot invest in a house abroad. c)Yes, he can buy a house abroad but the maximum remittance per calendar year is USD 100,000 under LRS. d)Yes, he can buy a house abroad. Maximum remittance per FY is USD 200,000 under LRS
54) Mr. Amrit says that he will definitely make a remittance in the next few months towards the house purchase within the permitted limit. However, he is worried that the Dollar: Rupee rates are not moving in his favour:
a)He can book a forward contract for USD 200,000 b)He can book a forward contract for USD 100,000 c)The maximum tenor of the contract is 12 months d)He should be informed of both a & c .
55) Mr. Anand is a NRI living in Richmond, U.S.A. Currently he is on a visit home. He has saved money in dollars in FCNR deposits maturing in three months time. He wishes to know whether he can book a Forwarrti^F contract to receive the maturity proceeds in GBP. He also wants to know whether the Bank can make a remittance in GBP on maturity date to a third party directly (to his son studying in London School of Economics).: a)No, he cannot book a Forwara contract and has to receive the proceeds in dollars only. b)Yes, he can book a Cross currency forward contract such that the proceeds can be paid in GBP. c)Bank can pay in GBP but to him only.d)Bank can make a direct remittance to his son in GBP as third party remittances are now allowed. e)Mr. Anand has to be informed of b & d
56) Mr. Mohandas from Omni exports wanted to know whether the interest subvention is applicable to his packing credit. His firm deals with manufacture of pickles and has an original investment of Rs.4 crore in plant and machinery:a)Yes, interest subvention of 2% applicable because it is food-processing industry b)No, interest subvention not applicable. c)Yes, interest subvention is applicable because it is a SME unit. d)Interest subvention scheme has been scrapped now.
57) Mr. Mohandas also wanted to know if he can give some credit (time to pay) to his buyers abroad. He has sent his export bill on collection bask through the Bank. His unit is situated in the vicinity of the branch and not in SEZ:a)Yes, time limit for realization of export proceeds is 180 days b)Yes, time limit for realization of export proceeds is 12 months c)Yes, time limit for realization of export proceeds is 15 months. d)Yes, there is no time limit for realization of export proceeds now for all exporters.

ANSWER

1	E	2	E	3	A	4	E	5	A	6	E	7	D
8	B	9	D	10	B	11	B	12	E	13	A	14	C
15	C	16	A	17	E	18	E	19	E	20	B	21	B
22	A	23	B	24	B	25	B	26	E	27	D	28	A

29	D	30	D	31	D	32	D	33	D	34	A	35	C
36	C	37	B	38	B	39	B	40	A	41	B	42	B
43	A	44	B	45	D	46	D	47	B	48	D	49	A
50	B	51	B	52	B	53	D	54	D	55	E	56-C, 57-B	

PRACTICE TEST PAPER NO. C (TEST YOUR SELF)

(MEMORY BASED RECOLLECTED QUESTIONS PREVIOUS YEAR)

1) Banks must augment their provisioning cushions to ensure that their total provisioning coverage ratio, including floating provisions, is not less than by September 2010. Provisioning Coverage Ratio (PCR) is the ratio of provisioning to gross NPA and indicates the extent of funds a bank has kept aside for covering loan losses.: a) 50% b)60% **c)** 70% d) 100%

2) As per current guidelines, the plan of realization for reconstruction of assets by a Securitization or Asset Reconstruction Company should not exceed five years from the date of acquisition of asset. RBI in the revised guidelines has extended the time frame___years.: a) 6 b)7 **c)** 9 **d)** 10

3) As per Nayak committee, the margin contribution of the Small Mfg Enterprises is % of annual projected turnover a) 5% b)10% c)Rs 20% 0) 25% e) None

4) As per the second method of lending of Tandon Committee, the Current ratio should be:
a) Less than 1 b)Exactly 1 c)More than 1.33 d) 1.33 e) 1.17:1

5) The Exposure Ceiling limits for banks would be_____percent of capital funds in case of single borrower and_____ % of capital funds in the case of a borrower group.: a) 40, 15 b)15, 40 c)20, 50 d) 50, 20

6) On scrutiny of a Balance Sheet of Mis Techno Inc, you observe that the long term uses of funds are more than long term sources. The position of the Balance Sheet indicates: **a)** Negative Net Working Capital b)Positive Net Working Capital c)Negative Working Capital Gap d) Positive Working Capital Gap e) None of the above

7) SARFAESI Act 2002 is not applicable in : a)Any security interest not exceeding Rs 1 lac. B)Any security interest in agriculture land c)Pledge of movable as per Section 172 of Contract Act d)Rights of unpaid seller under Section 47 of Sales of Goods Act e)All of the above

The Balance Sheet of M/S Vipin & Co reveals that the capital and free reserves are Rs 12 lac, term loans from banks for Rs.22 lac, CC (Nye) limit from bank showing balance outstanding of Rs 10 lac, sundry creditors of Rs 10 lac and provisions of Rs 6 lac. On the assets side. fixed assets are Rs 15 lac, non-Current assets are 3 lac, preliminary and pre-operative expenses Rs. 2 lacs and Current assets Rs 40 lac (cash Rs 2 lac, sundry debtors Rs 13 lac, stocks Rs 25 lac). The Profit & Loss statement shows following important operational results:

-Sales : Rs 100 lac.
-Purchases : Rs 80 lac,
-Net profit : Rs 5 lac.
-Number of units sold : 1 lac units
-Total Fixed cost Rs 4.5 lac.
-Total Variable cost : Rs 90.5 lac

8) The Creditor's velocity ratio is: a) 1 month b)1.5 months c)2 months d) 2.5 months

9) The Net Working Capital is : al Rs 10 lac b)14 lac c)Rs. 16 lac d) 18 lac

10) The Working Capital Gap is: a) Rs 20 lac b)Rs 24 lac c)Rs 26 lac d) Rs 28 lac

11) Working Capital turnover ratio is: al 1.5 times b)*2* times c)2.5 times d) 3 5 times

12) Accumulated losses are to be classified as:
a) Fixed liability b)Rolling liability c)Concurrent liability d) Current liability e) Fictitious Assets

13) In the Keynes model above, which is independent?:
a) Investment b)Consumption c)National income d) Consumption and investment

14) The domestic Commercial Banks have a target of ____ % for total priority sector measured as a percentage of ANBC or CE-OBE whichever is higher.: a) 32% b)50% c)18% d) 40%

15)___of Small Enterprises advances should go to the Micro Enterprises: a) 60% b)40%c)25% d) 50%

16) In which of the following kinds of financing, the banks take up financing exposure for medium term (5.7 years) out of the very longterm nature of the projects (15.20 years):
a) Take Out financing b)Securitisation c)Project participation d) Consortium

17) Debt Equity denotes position of the firm: a) Profitability b)Solvency c)Liquidity d) None

18) In a Balance Sheet, profit is shown under: a) Liabilities b)Current assets c)Fixed assets d) None
19) Limitation period in case of Cash Credit Pledge Aic is: a)3 years from the date of pledge
b)3 years from the date of documentation c)5 years from the date of legal notice d) No limit
20) A Micro Mfg Enterprise had been sanctioned CC(Hyp) limit of Rs 10 lac with 20% margin against paid stocks. The unit submits stock statement, which indicates the value of stocks as Rs. 14 lac with sundry creditors to the extent of Rs 9 lac. What will be the drawing power": a) Rs 1 50 lac b)Rs. 2 lac c)Rs 4 lac d) Rs. 6 lac
21) Accumulated loss will be deducted from: a) Paid-up capital b)Surplus capital c)Tier I capital d) Tier II capital
22) The Corporate Debt Restructuring Scheme (CDRS) introduced as per Vepa Kamesam committee has been modified under a special group headed by RBI Dy Governor Smt S.Gopinath. Accordingly, the scheme's scope has now been extended to cover entities having multiple banking exposure with outstanding exposure of Rs _____crores and above.: a) 10 b)20 c)5 d) 15
23) Category - Ii, CDR is meant for cases where the alcs have been classified as_____in the books of creditors:
a) Standard b)Substandard c)Doubtful d) Loss
24) What is the minimum & maximum denomination amount for a Commercial Paper?:
a) 5 lac. 5 lac b)10 lac. 5 lac c)10 lac, 10 lac d) 5 lac. 10 lac e) None of above
25) Recession is associated with fall in: a) Demand b)Supply c)Disinvestment d) Investment
26) Devaluation means: a) Fall in Marginal utility of Money b)Fall in printing of currency
c)Risk in black money d)Fall in the value of money in terms of foreign currency
27) From the Bank's perspective, the main difference between extending a Term loan and extending a Deferred Payment Guarantee is: a)In Term loan, Bank faces outlay of funds b)In DPG Bank faces inflow of funds c)a & b d) Neither a nor b
28) Marginal utility curve of a given consumer is also his:
a) Indifference curve b)Demand curve c)Supply curve d) Total utility curve
29) The total utility is maximum when: a) MU is zero b)AU is the highest c)MU is the highest d) MU is equal to AU
30) How many motives for demanding money has been given by Keynes: a) 1 b)2 c)3 d) 4
31) In calculating a country's GNP at market prices one of the following is not included:
a) Depreciation b)Net factor income from abroad c)Net indirect taxes d) Transfer Payment
32) Indian Economy can be best described as:
a) Developed economy b)Undeveloped economy c)Developing economy d) Underdeveloped
33) The open market operations (0M0) refer to the sale and purchase by the RBI of:
a) Foreign exchange b)Gob c)Government securities d) All of the above
34) Which of the following is a direct tax?: a) Sales tax b)Entertainment tax c)Excise duty d) Estate duty
35) Capital deficit in India is: a) Positive b)Zero c)Negative d) None of the above

ANSWERS

1	C	2	B	3	A	4	A	5	B
6	A	7	E	8	B	9	B	10	B
11	C	12	E	13	A	14	D	15	A
16	A	17	B	18	A	19	D	20	C
21	C	22	A	23	C	24	A	25	A
26	D	27	A	28	B	29	A	30	C
31	D	32	C	33	D	34	BD	35	A

PRACTICE TEST PAPERS

TEST YOURSELF - 01

Read the following statement carefully : (1) In a no. of economies, most of the economic issues are settled by the market mechanism of demand and supply where individuals and firms make the major decision about production and consumption. (2) In certain economies, the decisions regarding production and consumption are taken by the govt. Ownership of most of the means of production are with the govt. (3) In certain economies, the economic decisions regarding production and consumption are taken by the individuals and firms within a framework of regulation put in

place by the goyt.
Based on this, answer the following questions:
1)The description of economy given as S.No.3, is that of a: A) market economy / capitalistic economy, B)socialistic economy / command economy C) mixed economy D) regulated economy
2) The features of an economy given at S.No.2 are that of a: A) market economy / capitalistic economy B)socialistic economy / command economy C) mixed economy D) regulated economy
3)The features of market economy / capitalistic economy have been given above at S. No
A) 1 B) 2 C) 3 D) none of the above
4)Which of the following statement is correct
A) study of gross domestic product is part of micro-economics B) study of individuals and firms is part of macro-economics C) the term 'ends' in micro-economics, refers to wants D) none of the above is correct
5)You are given the following information

Combination	Price in Rs.	Quantity Demanded
A	800	300000 Units
B	700	400000
C	600	500000
D	500	600000
E	400	700000

06) The information given above in the Table is called: A) demand B) law of demand C) demand schedule D) price and demand
07)From the given information, it can be concluded that:
A) there is application of law of demand B) application of law of demand is not visible in the given example C) Demand has been declining D)demand has been rising as price is rising
08)If a demand curve is drawn on the basis of this information, the movement of the curve will be
A) left to right downward B)left to right upward C) parallel to X axis D)parallel to Y axis
09) Simple interest is calculated as:
A) principal x rate B) product x rate x time C) principal x rate x time D)principal x time
10)Compound interest is paid on which of the following:
A) principal amount B)interest amount C) principal amount and interest already accrued D) principal amount and interest to accrue
11)If interest is to be compounded monthly, which of the following will be used:
P (l+r)^{nB} P (1+r/2)^{nx2C} P (i±r m)1X 4D p (i+r /l e x 1 2
12) In a compound interest equation P = Ae^{rt} e, the exponential number is approximately:
A)2.82776 B) 2.71728 C) 2.77221 D) 2.82179
13) **Which of the following formulae can be used for calculation of equated monthly installment (EMI)?**
A) P x r[(l+r)^{n} x (l+r)^{n} —1] B) P x r [(l+r)^{n} / (l+r)^{n} +1] C) P x r [(l+r)^{n} / (l+r)^{n} —1] D) P x r [(l+r)^{n} / (l+r)^{n}]
14)Repayment of house loan installment for a pre-determined period on EMI basis is an example of
A) single cash flow B) annuity C)perpetuity D) any of these
15) Z rented his house for 2 years at a monthly rent of Rs.15000 to be received in advance. This is an example of?
A)ordinary annuities B) annuities due C) initial annuities D) base period annuities
16) Z is to invests Rs.100000 by end of each year for 5 years at 5% rate of interest. How much amount he will receive?
A) Rs.555236 B)Rs.562461 C) Rs.552563 D) Rs.526477
17) XYZ purchased machinery of Rs.100000. Rate of depreciation is 10%. At WDV value method, what is the amount of depreciation for 4 years. A) 34390 B) 33291 C) 33109 D) 33012
18) A person wants to receive Rs.1250 every quarter for 5 years at 12% p.a. rate of interest. How much he should invest now. A) Rs.18969.85 B) Rs.18956.58 C) Rs.18596.85 D) Rs.18695.85
19) X wants to receive a fixed amount for 15 years by investing Rs.9 lac at 9% interest rate. How much he will receive annually. A) Rs.101659 B) Rs.110983 C) Rs.111653 D) Rs.114282
20) To calculate value of a sinking fund, which of the following formulae can be used:
A) A [{ (l+r)" -1} / r] B) A/[{(1+0"-1}/r] C) A [{ (1+0^{11}+1} / r] D) A [(l+r)"-1} x r]
21) X wants to send his daughter to a management school after 5 years and will be needingone time payment of charges amounting to Rs.7 lac. At 12%, how much he should invest annually?
A) Rs.111105.21 B) Rs.110186.81 C) Rs.109672.22 D) Rs.109486.89
22) X obtained a loan of Rs.92820 at 10%, which he is to pay in 4 equal annual instalment. Calculate the amount of instalment? A) Rs.28283 B)Rs.29282 C) Rs.29476 D) Rs.29822
23) The Landmarks of Tomorrow, a book on human resources management has been authored by:
A) Peter.Drucker B)Edgar Schein C) Frederick Taylor D) Abraham Maslow

24)In the years 1856-1915, who conceptualized and pioneered the scientific management approach
A) Charles Babhage B) Robert Owen C) Frederick Taylor D) Abraham Maslow
25)Which of the following is part of human resources management (HRM):
A) routine functions B) organizational development C) employee development D) all the above
26)The HR professional's role includes creating necessary culture and values in the organization, diagnosing the problem at organization level and taking corrective steps. These fall, in which of the following category:
A) role of developing competence B) process role C) supportive role D) supportive role
27)Which of the following statement is correct?
A) HR functions in banks are generally performed professionally like other corporates B) HR functions in banks are generally performed professionally like other corporatesC) HR functions in banks are generally not performed professionally like other corporatesD) HR functions in banks are professionally performed unlike other corporates
28)Which of the following enhanced the role of HR professional (1) growth of unionism (2) state interventions through a no. of legislations (3) stress on statutory welfare A) 1 to 3 all B) 1 to 3 all C) 2 and 3 only D) all
29)Which of the following aims at safeguarding interest and controlling exploitation of specific groups (1) Child Labour Act 1986 (2) Bonded Labour System Act 1976 (3) Interstate Migrant Workmen Act 1979.
A) 1 to 3 all B) 1 and 3 only C) 1 and 2 only D) 2 and 3 only
30)In the present context, the objective of HRD (which one is correct)
A) to develop capabilities of each employee as an individual to B) develop team spirit and functioning in every organizational unit C) collaboration amongst different groups in the organization D) all the above
31) The first decade of 21^{5}' century saw extensive competition in the banking activity due to (1) liberalization (2) globalization (3) deregulation. (4) privatization A) 1 to 4 all B) 1 to 3 only C) 2 to 4 only D) 1, 3 and 4 only
32)Job role or job analysis comprises
A) job description only B) job description and job evaluation only C) job specification and job description only job D) description, job evaluation and job specification
33)_____ is primarily used to compare similarity between jobs within an organization or between organisations or even in an industry: A) job description B)job role or job analysis C) job specification D) job evaluation
35)As per explanation of the need hierarchy, need for an individual to realize his potential and self-actualization is as strong as satisfying physical needs.A) Robert Owen B)Charles Babbage C) Abraham MaslowD) Douglas McGregor
36)According to Nadler, the learning for growth of the individual not related to a specific present or future job is known as: A) training B) education C) development D) seminar
37) Whose work can be cited as the first instance of defining the perspective of adult learning in the 20thcentury:
A) Socrates B)Confucius C) Lindeman D) Aristotle
38)In the history of credit flow from banking system to the poor persons of society, the was a major event:
A) opening of bank branches B) nationalization of banks in 1969 C) selective credit control of RBI D) all the above
39)The trusts can be regulated by (a) Indian Trust Act (b)Public Trust Act (c)Religious and Charitable Endowments Act (d) Wakf Act A) a to dall B) a and b only C) a and c only D) a, b and d only
40)Which of the following category is required to be adopted by banks as business segment for public reporting purposes, as per RBI guidelines (a) treasury (b)corporate/wholesale banking (c)retail banking (d) other banking business A) a, b and c only B)a and d only C) b and c only D) a to d all
41) As per low value of individual exposure criterion for retail banking segment, the maximum aggregate exposure, to one counterparty should not exceed: A) Rs.1 cr B) Rs.2 cr C) Rs.3 cr D) Rs.5 cr
42)The working capital limits such as cash credit or overdraft can be used for which of the following purposes
A) purchase of fixed assets B) investments in other firms and companies
C) purchase of current assets D) investment in capital market
43)Lending target for agriculture within priority sector is (which one is not correct) A).18% ANBC or credit equivalent of off-balance sheet exposure whichever is higher B).25% of priority sector C) for foreign banks there is no target for such advances D).indirect advance is also part of agriculture subject to certain conditions.
44) Within 60% target for micro enterprises within MSE advances, there are further targets for micro enterprises. Which of the following is correct: A) 40% points out of 60% points, should be given to micro enterprises with investment in plant and machinery and equipment up to Rs.5 lac B) 40% points out of 60% points should be given to microenterprises with investment in plant and machinery and equipment up to Rs.2 lac C) 20% points out of 60% points, should be given to micro enterprises with investment in plant and machinery and equipment above Rs.5 lac D) 20% points out of 60% points, should be given to micro enterprises with investment in plant and machinery above Rs.5 lac and equipment above Rs.2 lac
45)For a small enterprise in manufacturing, which of thefollowing investment criteria is correct:
A) investment in equipment above Rs.25 lac but up to Rs.5 crB) investment in plant & machinery of Rs.25 lac but up to Rs.5 crC) investment in equipment of Rs.25 lac but up to Rs.5 cr, D)none of the Above
46)Which of the following can be included in micro credit:
A) aloans of very small amount not exceeding Rs.25000 B) loans of small amount not exceeding Rs.50000 C) loans of amount up to Rs.1 lac D) loans of small amount up to Rs.20000

47)Advances allowed by banks to directors can be written off (remitted) by banks:
A) under provisions, of Section 20 (*A)* of Banking Regulation Act B) under provisions of Section 20 (*A)* of Banking Regulation Act with permission of RBI or Govt. C)under provisions of Section 20 (*A)* of Banking Regulation Act with permission of RBI D) cannot be written off at all
48)Which of the following statements is not correct with regard to Selective Credit Control directives of RBI:
A) objective of directives is to prevent speculative holding of essential commodities with the help of bank credit B) presently the directives are applicable on pulses, food grains, oil seeds etcC) bank have been given discretion to consider advances against sensitive commodities D) selective credit directives are still applicable on buffer stock of sugar with sugar mills and unreleased stocks of sugar with sugar mills representing levy sugar and free sale sugar
49)Under group exposure norms of RBI, the ceiling on such credit exposure in respect of single borrower is:
A) 15% of the capital fund of the bank which can be relaxed to additional 10% for infrastructure projects. B) 15% of the capital fund of the bank which can be relaxed toadditional 5% for infrastructure projects. C) 15% of the net worth of the bank which can be relaxed to additional 5% for infrastructure projects D) 15% of the capital up capital + reserves of the bank whichcan be relaxed to additional 5% for infrastructure projects.
50)beneficiary of an LC wants to negotiate the documents under LC with a bank other than his own bank. Which of the following are RBI guidelines in such cases
A) since bills are being negotiated under LC, such transactions can be encouraged B) since this restrict the cash flows to the loan accounts of the bank which is regular bank of the beneficiary, banks should not encourage such negotiations to non-constituents C) since LC is opened as unrestricted, the banks may allow such facilities D) none of the above

Answers Test No.1

01	c	02	ʳb	03	a	04	c	05	c
06	a	07	a	08	c	09	c	10	c
11	d	12	b	13	C	14	b	15	b
16	c	17	a	18	C	19	c	20	a
21	b	22	b	23	A	24	c	25	a
26	b	27	c	28	A	29	a	30	a
31	d	32	d	33	D	34	d	35	c
36	c	37	c	38	B	39	a	40	d
41	d	42	c	43	B	44	d	45	d
46	b	47	c	48	B	49	b	50	B

TEST YOURSELF - 02

You are provided the following information:

Situation	Price	Demand	Supply
1800	300000	900000	
2	700	400000	700000
3	600	500000	500000
4	500	600000	300000
400	700000	200000	

1) On the basis of given information, what is equilibrium price demand and supply
A) 800, 300000, 900000 B) 700, 400000, 700000C) 600, 500000, 500000 D) 500, 600000, 300000
02) In situation (1) in the given Table, to reach equilibrium, the:
A) the price should increase, demand should increase, supply should increase B) the price should decrease, demand should increase, supply should decrease C) the price should decrease, demand should increase, supply should increase D) the price should increase, demand should decrease, supply should increase
03) Find out which is not a correct statement
A) demand schedule is the relationship between price and quantity sold B) market demand curve has downward sloping position C) when a factor other than price brings change in the supply, it is called shift in supply D) market clearing price is another name for equilibrium price
04)Demand deposits of banks are not included in which of the following for the purpose of money supply aggregates:
A) M O B) M 1 C) M 2 D) M 3
05) Average income of the population in the country has increased by 15%. The demand for a commodity sat X will:
A) increase B)decrease C)increase, if it is a superior commodity and decrease if it an inferior commodity

D) decrease, if it is a superior commodity and increase if it aninferior commodity
06) The shift in demand would not occur in the following cases:
A)price of X has increased leading to decline in demand B) demand for cold drinks has declined during winter season C) demand for consumer durables increased due to increase in income of the consumer D) demand for ink has declined due to increase in cost of pen.
07)In the context of cost of production which of the following statement is not correct:
A) if production cost for a commodity is low in relation to its market price, the producers would like to produce more and sell more B) if production cost for a commodity is high in relation to its market price, the producers would like to produce less and sell less C) if production cost for a commodity is low in relation to its market price, the producers would like to produce less and sell less D) none of the above
08)• Supply of a commodity is affected (which is correct statement):
A) if price of a substituted commodity declines B) if price of a substituted commodity increases C) if price of a complimentary commodity increases D) all the above are correct.
09) Debts can be active or passive. Which of the following explanation matches in this context:
A) active debts means which we owe B) passive debts means what is due to us C) passive debts means which we owe and active debts means what is due to us D) active debts means which we owe and passive debts meanswhat is due to us
10) The present value of a bond is equal to:
A) the amount of interest it will earn B) the amount of future cash to be received in future till maturity of the bond C) the present value of cash to be received in future tillmaturityof the bond D) the amount to be received on maturity
11) A bond has been issued with a face value of Rs.20000 at 12% coupon for 3 years. The required rate of return is 10 %. What is the value of the bond? A) Rs.20689.70 B) Rs.20988.80 C) Rs.20898.30 D) Rs.20918.40
12) Current yield of a bond can be calculated as under: A) current interest / current market price B) coupon interest / face value C) coupon interest / current market price D) current interest / face value
13) A 10%, 6 years bond, with face value of Rs.1000 has been purchased by Z for Rs.900. What is his yield till maturity A) 12.50% B) 12.20% C)11.80% D) 11.60%
14)When the required rate of return is less than the coupon ratethe value of the bond is :
A) less than face value B) more than face value C)equal to face value D)maturity value
15) For a given difference between the YTM and the coupon rateof a bond, the longer the term to maturity, the with a change in YTM: A) smaller will be the change in the price B) greater will be the change in the price C) greater will be the change in the maturity value D) smaller will be the change in the maturity value
16) A change in the YTM affects the price of the bonds with aYTM more than it does the price of bonds with a YTM. A) lower, higher B) higher, lower C) lower, lower D) higher, higher
17)X purchased a Bond with face value of Rs.1000 and coupon of 8% and maturity of 6 years. If YTM is increased by 1%, the change in price of Bond-2 would be: A) Rs.44.83 increase B) Rs.44.83 decrease C) Rs.48.33 increase
D) Rs.48.33 decrease
18) Z invested in 10% 3 year bond of face value of Rs.1000 each. The expected market rate is 12%. What is the duration of the bond A) 2.73 years B) 2.93 years C) 2.63 years D) 2.83 years
19) An increase in the frequency of coupon payments duration and a decrease in frequency of coupons
A) decreases, increases B) decreases, decreases C) increases, increases D) increases, decreases
20)D x YTM/1 + YTM gives: (D means duration and YTM means yield to maturity)
A) duration of the bond B)bond price elasticity C) yield to maturity of the bond D) interest rate elasticity
21) Z purchased 8%, 5 years bonds of Rs.10 lac, with annual interest payment and face value payable on maturity. The YTM is assumed at 6%,. Calculate percentage change in the price of the bond when the decrease in YTM is 100 basis points from 6% to 5% and the duration is 2.79% and modified duration is 2.63%
A) 2,63% B) 2 . 7 3 % C) 2.83% D) 2 . 9 3 %
22)Z is to receive Rs.60000 from bank at the end of 3 years, being the maturity value of a term deposit. How much he is depositing now, if the interest rate is 10%? A) Rs.44097 B) Rs.45079 C) Rs.47075 D) Rs.49059
23)Learning occurs when learners have the freedom to learn, what is particularly relevant to their personal life situation. It is stated by which of the following theory:
A) mechanistic theories B) cognitive theories C) organismic theories D) behaviourist theories
24) The training needs can be identified by an organization on the basis of (1) performance appraisal (2) productivity norms fixed by the organization (3) larger rejects for the job done by the employee (4) inspection reports
A) 1 to 4 all B) 1 to 3 only C) 2 to 4 only D) 1, 3 and 4 only
25) While conducting the training programs, which of the following methodology is used:
A)lectures and experimental lectures B) reading and discussions C) case studies and role plays D) all the above
26)The evaluation of training is done at 4 levels. At one of these levels, the participants learn knowledge, skills and attitudes about the subject matter, which is evaluated through some test conducted before and after the training. This level is called: A) reaction level B) learning level C) behavior level D) functioning level
27)The trainer in a bank should be: A) practicing managers only B) operational people only C) specialists recruited as

core faculty only D)a mix of practicing managers, operational people andspecialist recruited as core faculty.
28)The persistent tendency to feel and behave in a particular way, towards some object, is called:
A) behavior B) attitudeC)habit D) any of the above
29) Which of the following components of attitude, involve the feeling of an employee or their affect-positive, neutral or negative-about an object:A) emotional B) informational C) behavioral D) all the above
30)Which of the following function is served by the attitudes (1) the adjustment function (2) the ego-defensive function (3) the value-expression function (4) the knowledge function.A)1 to 4 all B)1 to 3 only C) 2 to 4 only D) 1, 3 and 4 only
31)Which of the following can play a great role in attitude change (1) friends (2) peers (3) opinion leaders a1 to 3 all A) 1 and 2 only B) 2 and 3 only C) 1 and 3 only
32) A stage when a person attempts to achieve ego integrity by examining whether life has been meaningful or satisfying, in the context of career planning, is called: A)adolescenceB)young adulthoodC) adulthood D) maturity
33) According to Dalton, Thompson and Price, in the career path, which of the following is required to define the direction in which the entire organization or at least a majorsegment of the organization would develop:
A)apprentice B)colleague C) mentors D) sponsors
34)According to Driver, in the an individual takes a new job, works hard, performs well, moves up in status and rank and then moves on to another type of work and follows the same pattern of development and performance.
A) steady state careers B) transitory pattern C) spiral career D) plateau career
35) Under career pattern, Schein has given comprehensive framework of 3 dimensional movements. The movement is along the hierarchy of the organization A) vertical B) circumferential C) radial D) cervical
36) According to Schein, there are _____type of career anchors A) two B) three C) four D) five
37)Which of the following career anchor category, as per Schein concept, does not match
A) some individuals want to create something new – autonomy B) some individuals are not comfortable with organization life They like to start something and want to make it a success autonomy C)some individuals want to create something new – creativity D) none of the above
38)The loan system of credit delivery is not applicable in case of: A) activities cyclical and seasonal in nature activities B) carrying higher risk weight activities carrying lower C) risk weight activities which are of regular nature
39)What is the maximum exposure a bank can have for equipment leasing, hire purchase or factoring services:
A) total exposure to these cannot exceed 10% of total advances B) exposure to each of these cannot exceed 10% of total advances C) exposure to each of these cannot exceed 15% of total advances D total exposure to these cannot exceed 15% of total advances
40)The objective of introducing Base Rate by RBI is (a) at enhancing transparency in lending rates of banks (b)enabling better assessment of transmission of monetary policy (c)keeping interest rates low.
A) a to c all B) a and b only C) a and c only D) b and c only
41) For which of the following category of loans the bank canlend at below base rate?
A) corporate loans B) priority sector loans C) loans below Rs.2 lac D) none of these
42)What is the periodicity of charging interest in loans by banks:
A) monthly basis B) quarterly basis C) half-yearly basis D) at discretion of banks
43)Which of the following is an basic financial statements (a) balance sheet (b)profit and loss account (c)funds flow statement (d) statement of bank account A) a to d B) a to cC) a, c, d D)a and b
44)When, the promoter of a business withdraws certain goods from the business for his personal use, his drawing account is debited. This is done due to application of :
A) going concern concept B)cost concept C) business entity concept D) realization concept
45)In a business firm, the assets = capital + liability: It is due to
A)going concern concept B) moneymeasurement concept C) matchingconcept D) dual aspect concept
46)The concept makes a distinction between the receipt of cash and right to receive it or payment of cash and obligation to pay cash: A) realization system B) cash concept C) accrual concept D) consistency concept
47)The books of business should be closed and reopened after regular time period as per:
A) consistency concept B) business entity concept C) going concern concept D) accounting period concept
48)The assets and liabilities are placed just opposite each other in case of
A)common-size statement system B) horizontal form of balance sheetC) vertical form of balance sheet D)a and b both
49)Which of the following is correct order in which the companies classify their liabilities:
A) share capital, reserves and surplus, secured loans, current liabilities and provisions, unsecured loans B) share capital, reserves and surplus, unsecured loans, securedloans, current liabilities and provisions C) share capital, reserves and surplus, secured loans, unsecured loans, current liabilities and provisions D) reserves and surplus, share capital, secured loans, unsecured loans, current liabilities and provisions
50) Which of the following is not part of secured loans raised by a company
A)inter-corporate borrowing B)debentures C) term loan from a bank D) term loan from a financial institutions

Answers Test No.2

01	c	02	b	03	A	04	a	05	c
06	a	07	c	08	B	09	c	10	C
11	b	12	c	13	A	14	b	15	B
16	b	17	b	18	A	19	a	20	D
21	a	22	b	23	C	24	a	25	D
26	b	27	d	28	B	29	a	30	A
31	a	32	d	33	D	34	c	35	A
36	d	37	a	38	A	39	b	40	B
41	d	42	a	43	D	44	c	45	D
46	c	47	d	48	B	49	c	50	A

TEST YOURSELF - 03

1) Bank term deposit with original maturity of 2 years and residual maturity of 8 months will be placed as part of:
A) MO B) M1 C) M2 D) M3

2)In money supply aggregation, the currency with public is calculated as
A) equal to currency in circulation) currency in circulation plus cash in RBI currency chest C) currency in circulation less cash balances with banks D) currency in circulation plus cash balances with banks

3) Which following is a positive of the effect of inflation:
A)increase in real income B) decrease in prices C) mitigation of economic recession D) all the above

4)Due to heavy demand of goods as a result of festive season, the prices of certain commodities in general, have increased.this is called A) cost push inflationB)headline inflation C) demand pull inflation bam7D)wholesale inflation

5)Which of the following is not a correct statement: money supply refers to the amount of money in circulation in the economy A) currency with public, demand deposits and other deposits B) with RBI is called broad money C) time deposits are not payable on demand.D) none of the above

6)If the current interest rates are low, the people will be reluctant to hold large quantity of bonds because of theinherent fear that bond prices would fall in future, causingcapital losses. This is stated by:
A)Keynes' Liquidity preference theory B) Hicks-Hansen synthesisC) Modern Economists D) Classical Economists

07)Which of the following statement is not correct:A) bond prices and current rate of interest are positively related as per JM Keynes B) Interest is the income from capital C) supply and demand analysis explains the rate of interest as a price, determined by the demand for money and supply of loans D) none of the above

08)As per cyclical fluctuations A) boom is followed by another boom B) depression is followed by another depression C) boom is followed by depression and depression is again followed by boom D) during boom period capacity is not fully utilized.

09) An investor invested Rs.7.50 lac in a project that gives profit of Rs.2 lac in the 1$^{5\backprime}$ year, Rs.2.60 lac in the 2nd year and Rs.4.50 lac in the 3rd year. At 10% discount rate, what is the present value of the cash inflows?
A) Rs.7.15 lac B) Rs.7.25 lac C) Rs.7.35 lac D) Rs.7.45 lac

10)Z made an investment of Rs.18000 and he expects a return of Rs.3000 per annum for 12 years. What is the present value of the cash flow at 15% discount rate? A) Rs.16263 B) Rs.16675 C) Rs.16968 D) Rs.17214

11 I)n statistics, the word is used to describe a portion chosen from whole lot of items:
A) parameters B) population C) sample D) statistics

17)When the population is normally distributed, the sampling distribution has standard deviation
A) population standard deviation x square root of the sample size B) population standard deviation / square root of the sample size C) square root of the sample size / population standard deviation D) square root of the sample size x population standard deviation

18)Estimate, with 95% confidence, the lifetime of nine volt batteries using a randomly selected sample where the sample mean X = 49 hours, sample standard deviation is s = 4 hours and no. of samples n = 36
A) 32.5 and 41.6 hours B) 39.1 and 45.7 hours C) 47.4 and 50.3 hours D) 49.8 and 53.1 hours

19)According to the distribution of annual earning of Juniorexecutives in a bank with 3 years experience, the distribution has a mean of Rs.500000 and standard deviation of Rs.120000. If a sample of 16 executives is drawn, what is the probability that the average earnings will be more than Rs.585000.
0.9126 A) 0 . 0 2 % B) 0 . 8 2 % C) 1.29% D) 3 . 9 3 %

20) In a sample of 36 observations from a normal distribution, with mean of 92.3 and standard deviation of 15.8, what is probability of P (87 < sample mean < 99). A) 0.8703 B) 0.9126 C) 0.9724 D) 0.9864

21)A credit card company observes that on average the monthly balance of any given customer is Rs.224 and the standard deviation is Rs.112. If 64 accounts are picked, what is the probability that the sample average monthly balance is between Rs.200 and Rs.260. A) 9.5130 B) 4.4061 C) 1.0436 D)0.9513
22)Under career path planning, at each level, the jobs which are comparable in terms of the knowledge, skill requirement can be identified and categorized as a group. This is called
A) task group B) job families C) work cluster D) any of the above
23) As part of the concept of self-development, the self can be categorized into 2 parts (1) patent self (2) explicit self (3) implicit self (4) inner self A) 1 and 2 B) 3 and 4 C) 1 and 4 D) 2 and 3
24)People work for a variety of reasons i.e. there are a no. of factors that motivate a person to work, which include the following: A) money and appreciation B)status C) work satisfaction, self-growth D) all the above
25)When an individual is of the view that the course of events is determined by one's own efforts and action and not due to external events or luck, this is called:
A) external locus of control) locus of control C)internal locus of control D)beyond control locus
26)Transaction analysis refers toA) understanding financial transactions B) uderstanding interpersonal relationship and interaction C) understanding transactions relating to business D) understanding transactions relating to business and ethic
27)Which of the following statement regarding 3 ego states in A) the ego states are unique to an individual B) the ego state is related to age of a person C) the ego state has no direct relationship to demographic parameter D) none of the above
28)Which ego state collects information and processes it. A) parent B) adult C) child D) a and b
29)What is the feature of a adult ego state, out of the following A) more of ethical, conscientious behavior and influenced by preaching from parents and elders. B)more of analytical, rational and practical orientation C) more of instinctive behavior with motive of enjoyment D) more of every thing
30)The _____ parent behavior criticizes others for theirundesirable behavior.
A)caring B) nurturing C) critical D) concerned
31)In his behavior, a person is displaying more of emotions than the facts. It can be classified as ego state:
A)parents B)elders C) adult D) child
32)Which of the following is a feature of a crossed transaction
A) from parents to child and again from parents to child B) it is undesirable C) the transaction is blocked D) all the above
33)According to Harris, what is the meaning of the life position, I am OK, you are not OK A) Both have value B) I have value but you do not have value C)I do not have value but you have value D) neither person has value
34)The objective of understanding the ego states profile of a person is:
A)to counsel him B) to make necessary modification in one's behavior C) to bring desired change D) all the above
35)In Johari Window, the window ARENA represents which of the following: A) known to self and othersB) closed to self and others C) known to others and not known to self D) known to self and not to others
36)For improving effectiveness in interpersonal relations, which of the following area is most critical
A)d a r k B) a r e n a C) blind D) closed
37)Net sales can be calculated as: A) gross sales minus excise duty or customs dutyB) gross sales plus excise duty or customs duty C) gross sales — sales returns D) gross sales + sales returns
38)Profit before tax is calculated as: A)operating profit + non-operating surplus B) operating profit - non-operating surplusC)operating profit + non-operating deficit D) none of the above
39)The bankers make analysis of financial statements with the objective of (a) assessment of performance and financial position (b)estimate for future performance (c)detection of dangersignals (d) assessment of credit needs (e) improving profits of the financed firm A) a, c and e B)b, c and e C) a, b and d only D) a to d all
40)Financial statements contain the percentage of a key figure alone without the corresponding amount figures:
A)trend analyzed B) funds flow C) common size D) ratio analyzed
41)As regards the debt equity ratio, the banks prefer:
A) high debt equity ratio B)increasing debt equity C)high and increasing ratio D) low and declining ratio
42)Debtor turnover ratio indicates which of the following:
A) how fast the loans are paid B)how quickly the loans are available C) how quickly the trade debtors are recovered D) how quickly the trade debtors are recovered
43)Which of the following is most important ratio to assess liquidity, for making assessment of working capital bank limits: A) debt equity ratio B)debt service coverage ratio C)current ratio D) working capital turnover ratio
44)The cash budget method is used where the amount of working capital limits is
A) Rs.1 cr or above B) Rs.2 cr or above C) Up to Rs. 1 cr D) none of the above
45) Under projected turnover method of Nayak Committee, the working capital operating cycle is equal to min _____projected sales A) one month B) one month C) three months D) four months
46) If the bank provides guarantee to the beneficiary that bank will reimburse the loss arising on account non performance or under performance of a contract by the customer (applicant), such guarantee is called:
A) deferred payment guarantee B) performance guarantee C) financial guarantee D)continuing guarantee

47) Which among the following is an important factor for determining the amount of LC limits for working capital purpose (a) average amount of each LC (b)frequency of opening the LC (c)amount of LC outstanding at a particular period. A) a and c only B) a and b only C) b and c only D) a to c all

48) The minimum and maximum time for which CP can be issued is

A) 15 days, 6 months B) 15 days, 12 months C)7 days, 6 months D) 7 day, 12 months

49)Term loans are repaid A) by sale of fmanced assets B) by additional contributions from promoters C) by future profits / cash generations from the project D)all the above

50)The term Knowledge Management refers to (which one is more appropriate):

A gaining knowledge B) creating knowledge and storing it C) a process of creating, storing, distributing and pooling the knowledge D) a process of converting knowledge into information

Answers Test No.3

01	D	02	C	03	C	04	C	05	B
06	A	07	A	08	C	09	C	10	A
11	C	12	B	13	D	14	C	15	C
16	A	17	B	18	C	19	A	20	C
21	A	22	B	23	C	24	D	25	C
26	B	27	B	28	B	29	B	30	C
31	D	32	D	33	B	34	B	35	A
36	B	37	A	38	A	39	D	40	C
41	D	42	C	43	C	44	D	45	C
46	B	47	D	48	D	49	C	50	C

TEST YOURSELF – 04

01)Which sector of Indian economy is having the lowest share in Gross Domestic Product out of the following:

A)industry B) agriculture C) services D) services and industry

02)The share of which of the following sectors in the economy, in overall GDP, has come down during the last 25 years: A) industry and services B) agriculture and industry C) services D) agriculture

03) Before opening up of the forex markets in India, the exchange earners (exporters) were required to surrender or purchase forex at:A) current market rates B) at reference rates fixed by RBI C) at foreign currency rates by FEDAI D) at forward rates less premium or discount.

04)As part of financial sector reforms, the previous office of Controller of Capital Issues has been replaced by:

A) CCI B) SEBI C) BCSBI D) CIBIL

05)Which of the following centersis the first in India, where the cheque truncation system has been introduced: A) Delhi B)Chennai C) Mumbai D) Bangalore

06) Which of the following features, is not correct regarding National Electronic Funds transfer:

A) it functions on a batch system B) the settlement takes place on a net basis C) it is a funds transfer as well as settlement system D) none of the above

07)Free and compulsory education to all children of 6 to 14 years of age, is a fundamental right. This provision was made by way of amendment to the Constitution of India: A) 80 B) 82 C) 84 D) 86

08)The term WMA stands for: A) why me alone B)ways and means advance C) weights and measures association D) wealth and money advances

09) Square root of (N-n) / N-1) where N is size of the population and n is the size of sample, gives us:

A)standard deviation B) standard error of the mean C)finite population multiplier D)infmite population multiplier

10) Fraction n/N is referred to by the Statisticians, as :

A) population fraction B) sampling fraction C) mean fraction D) standard deviation fraction

11)The city police is stopping every vehicle at a check point moving on a particular road, within the city. They are using (1) simple random sampling (2) stratified sampling (3) complete enumeration (4) systematic sampling

A) 1 and 4B) 2 and 4 C)only 4 D)only 3

12) A school wants to predict the no. of poor students who may get better scoring in the examination when they are given extra classes. This prediction is called:A)correlation B)regression C)standard error of estimate D)none of these

13)If the value of correlation is equal to 1, this means that: A) there is large inverse relationship between 2 variables.B) there is perfect inverse relationship between 2 variables.C) there is large positive relationship between 2 variables. D)there is perfect positive relationship between 2 variables.

14)If the value of correlation r = 0, it indicates:
A) perfect inverse correlation B)perfect positive correlation C)no linear correlation D) no correlation
15)Calculate the correlation coefficient based on the following data relating to demand and price:

Demand In quintals	65	66	67	68	70	72
Price InRs.	67	68	65	72	69	71

A) no correlation B)0.6812 C) 0.5781 D) 0.9221
16) In regression analysis, within the equation y = a + bx, *a is :*
A) the y-intercept B) the x-intercept C) The b-intercept D)indicator of slope of the line
17)You are given the following data:

DEMAND IN QUINTALS	65	66	67	68	70	72
PRICE IN RS	67	68	65	72	69	71

If the value of x = 80, find out the value of *y*
A)88.49 B) 75.29 C)64.08 D) Value cannot be calculated.
18)Which of the following represents the observed and predicted values and help to get the feel of the situation:
A)dependent variable B)scatter diagram C) trend analysis D) correlation analysis
19)The following information relating to no. of ships loaded in aharbour has been provided: 2005 (98 ships), 2006 (104 ships), 2007 (115 ships), 2008 (118 ships), 2009 (131 ships), 2010 (152 ships) and 2011 (174 ships). It is observed that there is increase in the no. of ships loaded over 7 years. Such variations come under which type of time series
A) secular trend B) cyclical fluctuation C)seasonal variations D) irregular variations
20)Of the 4 variations of time series, which represents the long term direction:
A) secular trend B) cyclical fluctuation C)seasonal variations D)irregular variations
21) Which of the following is the benefit to study the secular trend (1) historical pattern can be described (2) future change can be projected I(3) trend components and seasonal components can be separated. (4) accurate predictions can be made.
A) 1 to 4 all B) 1 to 3 only C)1 and 3 only D)2 and 3 only
22)Cyclical variation, as a component of time series, tends to oscillate above and below the secular trend line for how much time period: A)up to one year B) one year C)longer than one year D) longer than 2 years
23)Which of the following is a component of emotional intelligence (1) self-awareness (2) self regulation (3) self motivation (4) empathy (5) social skills A)1, 3 and 5 only B) 2 and 4 only C) 2, 3 and 5 only D) 1 to 5 all
24) Human behaviour is a complex phenomenon. It is result of many factors including (1) biological process (2) psychological process (3) social process (4) nformation process
A) 1 to 4 all B)1 to 3 only C) 2 to 4 only D) 2 and 3 only
25)Which of the following factors falls in organizational factors so far the influence on behavior of an individual is concerned: A)cultural, social, economic factors B) age, sex and education C) Personnel policies, reward and compensation system D) 'values, perception and attitude
26)The cabin of a bank branch manager gives an untidy look and messy appearance. His table is full of papers. He is exhibiting: A) type A behavior B)type B behavior C)a mix of type A and type B D)neither type A nor type B
27)Which theory of personality believes that the traits of a person which determine his personality and behavior, are basically inherent to a person:
A) Psycho-analytical theoryB) Trait TheoryC) Self concept theoryD) Social learning theory
28)_____theory of personality believes that the personality development is more a result of social variables than biological factors.A) Psycho-analytical theoryB)Trait TheoryC) Self concept theory D)Social learning theory
29)Split brain (right vs left) psychology is closely related to ESB. Which of the following is not controlled by the left side of the brain:A)speech B) emotions C) reading and writing D) sequential ordering
30)According to personality job fit theory of John Holland, there are 6 types of personality. Which of the following is not such personality (1) realistic (2) investigative () social (4) conventional (5) enterprising (6) artistic:
A)1 and 3 B) 2 and 5 C)6 only D) none of these
31)The human resources systems are largely designed by banks and other organizations for:
A) a heterogeneous workforce B)a homogenous workforceC) a diverse workforce D) according to their need
32) Which of the following approach acknowledges the existence of cultural distance and attempts to teach individual members about cultural differences through training:
A)diversity enlargementB) diversity sensitivity C)cultural audit D)all the above
33) The term motivation has been derived from:A) Roman word B)an English wordC) a Latin wordD)a Devnagari word
34) As per Abraham Maslow's motivation theory, the people have needs:A) 2 bB)3 C) 4 D) 5
35) Which theory on motivation observed that the opposite of satisfaction is not dissatisfaction and removing dissatisfying contents from job does not necessarily make the job satisfying.
A) Frederic Herzberg B) Elton Mayo C) A. Maslow D) V H Vroom
36)According to ERG theory, there are sets of needs in the organizations. A) 2B)3 C) 4 D) 5
37 I)n the balance sheet of a bank, the term loans and bank guarantees are shown as under:
A) term loan in the asset side and DPG on the liability side B) term loan and DPG both on the asset side C)DPG is

shown as a contingent liability and term loan as an asset D) none of the above

38)At times a small change in the price of one variable say, raw material, may impact the profitability drastically. This is examined through:A) break-even analysis B)sensitivity analysis C) profitability analysis D)all the above

39.) If a bank finances the promoters for acquisition of an infrastructure company, the maximum amount should be restricted to of finance required for acquiring promoter's stake in the company being acquired.

A)15% B)20% C) 25% D) 50%

40)Project loans can be allowed by banks to which of the following groups

A) infrastructure companies only B)any type of companies only C) companies, partnerships only

D) any entity engaging itself in productive economic project

41) What is the maximum amount of commission or brokerage fee that the borrowers can pay to the guarantors as consideration for the guarantee:A)0.25% of the guaranteed amountB)0.50% of the guaranteed amountC)0.75% of the guaranteed amount D) such payments cannot be made by the borrowers

42)If a borrower is availing working capital facilities with one bank and wants to open current account with another bank: A) it can do so at its discretion B) it can not do so in any circumstances C)it can do so with permission of the financing bank D) it can do so at the discretion of the bank, with whom it wants to open the account.

43) Under Loan system of Credit delivery, the permanent portion called working capital demand loan (WCDL) should normally be: A) 80% of the MPBF B) 75% of the MPBF C) 50% of the MPBF D) 20% of the MPBF

44) With a view to restrict the happening of frauds in consortium or multiple banking loans, RBI made it mandatory to obtain declaration from borrowers availing limits of and above, about limits availed from other banks:

A) Rs.5 cr and above)B Rs.10 cr and above C)Rs.15 cr and above D) Rs.20 cr and above

45) If a firm provides wrong information about its debtors to avail the cash credit limits, it can be detected with the help of A) receivable audit B) verification of receivables from books C)cross-checking of information from the balance sheet data D) all the above

46) If inventory (stock position) details are wrongly mentioned by a borrower, which of the following cannot be used to detect, incorrect mention of stocks in the stock statement:

A)analysis of balance sheet and profit/loss account B)stock audit C)physical verification of stocks D) cross-checking of information from the balance sheet data

47) Credit risk can be defined as: A)possible willful default by borrowers in meeting their loan repayment obligations B)possible genuine inability of the borrowers in meeting their loan repayment commitments C) possibility of loan account becoming NPA.s_ D) all the above

48) Which of the following is not part of micro level risk mitigation step: A) following policies where the risk is evenly spread over all geographical areas B)monitoring of individual loan account effectively C) following standards of appropriate loan documentation D)obtaining collateral securities to secure the loans properly

49)Which of the following is not a situation of credit risk:

A)willful default by the borrower in repayment of the loanB) inability of the borrower in repayment of the loan due to losses in the business C) invocation of guarantee by the beneficiary due to non- compliance by the borrower, on whose behalf the guarantee was issuedD)fraud committed by a borrower in connivance with the bank staff, not relating to the loan accounts

50) Which of the following does not match: A) IT has reduced the importance of human resources in the banks – false B) IT can effectively substitute the manual systems and no other change is required –false C) IT can be used in HRM to reduce the drudgery of accounting and preparing salaries – True D) The positive aspect of IT is that more people can be used for strategic decision making - True

Answers Test No.4

01	b	02	d	03	b	04	b	05	a
06	c	07	d	08	b	09	c	10	B
11	d	12	b	13	d	14	c	15	C
16	a	17	b	18	b	19	a	20	A
21	b	22	c	23	d	24	b	25	C
26	a	27	b	28	d	29	b•	30	D
31	b	32	b	33	c	34	d	35	A
36	b	37	c	38	b	39	d	40	D
41	d	42	c	43	a	44	a	45	D
46	a	47	d	48	a	49	d	50	C

TEST YOURSELF - 05

01)The term ITES relates to which of the following: A)information technology and enabled services B)information technology andelectronic services C)incoming technology and early solutions D)income tax and excise services
02) The goal before RBI is to help the economy to come out of ongoing depressed economic activity. What type of monetary policy it should follow:
A) tight money policy B) contractionary policy C) expansionary policy D) adhoc policy
03I)n a contractionary monetary policy, which of the following action is not initiated by RBI:
A) increase in CRR B) increase in Repo rate C) increase in interest rates D) none of the above
04)Which of the following is not an implication of increase in statutory liquidity ratio:
A) it helps in restricting the credit expansion B) it ensures the solvency of commercial banks C) it compels banks to invest more in govt. securities D)it ensures reduction in rate of interest in general
05)The rate at which the banks park their short term excess liquidity is called:
A) repo rate B)reverse repo rate C) bank rate D) base rate
06) When RBI finds that there is too much money floating in the banking system,which of the following is initiated by RBI: A)increase in repo rate B) increase in reverse repo rate C) undertaking of repo transactions
D) undertaking of reverse repo transactions
07)The fiscal policy has 2 main instruments:
A) budget and deficits B) fiscal deficit and revenue deficit C) expenditure and earning D) spending and taxation
08)Which of the following is not a tool of monetary policy?
A)open market operations B) ways and means advances C)repo rate D)bank rate
09) The sale under SARFAESI Act can be through:
A) private treaty B)public tender C)public auction D)any of the above
10)Banks that have declared a borrower as a willful defaulter, are required to send report to (which is not correct): •
A)RBI for non-suit filed cases with outstanding of Rs.25 lac and above on a quarterly basis i.e. Mar, June, Sept and Dec
B) CIBIL for suit-filed cases with outstanding of Rs.25 lac and above on a quarterly basis i.e. Mar, June, Sept and Dec
C)SEBI of all cases of willful defaulter on a half yearly basis i.e. Mar and Sept D) none of the above
11) When application is filed with DRT by the bank under provisions of RDDB Act, DRT sends notice to the defendant (borrower) within---------- as to why the relief should not be granted to the bank:
A) 7 days B) 15 days C) 30 days D) 45 days
12)A firm had estimated sales of Rs.25 lac for 2009, Rs.40 lac for 2010 and Rs.60 lac for 2011. The actual achievement is Rs.30 lac, Rs.40 lac and Rs.55 lac. What is relative cyclical residual for 2010 in this case:
A) 0 % B)100% C) 40 lac D)inadequate information
13)The index for measuring seasonal variation in time series, is based on
A) 0 B) 10 C)100 D) it varies from time to time.
14)Which of the following is a type of estimate (1) point estimate (2) interval estimate (3) range estimates (4) general estimate.A) 1 to 4 all B)1 and 2 only C) 3 and 4 only D) 1,3 and 4 only
15)Which of the features of a point estimate is not correct?
A) A point estimate is often insufficient B) a point estimate is either right or wrong C) a point estimate is much more useful if it is accompanied by an estimate of the error that might be involved.D) none of the above
16)Which of the following statement is correct (1) sample mean can be estimator of the population mean (2) sample mean cannot be estimator of the population mean (3) Sample proportion can be used as an estimator of the population proportion (4) Sample proportion cannot be used as an estimator of the population proportion
A)1 and 4 B)1 and 3 C)2 and 4 D)2 and 3
17) The sample size is increased. It is almost certain that the value of the statistic is very close to the value of the population parameter. This represents which of the following features of a good estimator:
A) unbiased B) efficiency C) consistency D)sufficiency
18)the bank branches maintains 10 very high networth individual deposit accounts. The balance in these accounts are (Rs in lacs

1	2	3	4	5
190	198	212	187	206

What is the standard deviation A)8.03 B) 6.80 C) 5.40 D) 4.70
19)the average life of flash light of car is 26 months and standard deviation is 5 months. If a sample of 400 cars is taken to know the range in which theaverage life falls calculate the range A) 26 months B) 24.2 months to 27.2 months, C) 25.6 months to 26.4 months D)information is not adequate
20) The simplex method in the linear programming is an iterative process which approaches an optimum solution in such a way that an objective function of maximization or minimization is fully reached. Which of the following statement is correct in this connection:

A) Each iteration in this process increases the distance (mathematically and graphically) from the objective function B) Each iteration in this process shortens the distance (mathematically and graphically) from the objective function. C) There is no change in the distance (mathematically and graphically) from the objective function. D) no statement can be drawn.

21) In linear programming, the slack variables enter the objective function but receive a coefficient of and do not influence the final result. A) 1.0 B) 0.5 C) zero D) -0.5

22) The optimum mix of a firm assumes a given set of constraints. If a constraint , a shadow price results and simply shows the change in the contribution margin per unit or in costs thereby results.

A) is added B) is relaxed C) is not changed D) none of the above

23) Dynamic programming is best suited for decisions that must be made in and that influence future decisions in the sequence.- A) promptness B) sequence C) emergency D) haste

24) India Manufacturing Company has several plants in different cities and serves customer in various other cities. It wants to know the best way to schedule shipments from various plants to various customers and has been advised that the problem can be solved using linear programming. In transporting cost minimization problem, the usual coefficients of the objective function would be: A) Usage rates for transportation facilities B) Restrictions on transportation facilities C) Shipping costs D) Time estimates for the critical path

25) In a system of inequalities for a linear programming model, to equalize an inequality such as 3x + 2y 15 what will be required to be done? A) Invert the inequality B) Add a slack variable C) Add an artificial variable D) Multiply each variable by -1

26) As, per on motivation, the motivation to act develops after a person compares the input / outcome with the identical ratio in comparison to the other person. A) Adam's Equity Theory B) Achievement Motivation theory C) Victor H Vroom theory D) Reinforcement Theory

27) -----means higher responsibility. It gives more decision making, planning and controlling powers.

A) job enrichment B) job enlargement C) job satisfaction D) job rotation

28) A set of expected behavior patterns attributed to someone occupying a given position in a social unit is called:

A) job B) role C) power D) assignment

29) The role set conflicts take which of the following Inns (1) role ambiguity (2) role expectations conflict (3) role overload (4) role erosion (5) role isolation A) 1 to 5 all B) 1 to 4 only C) 2 to 5 only D) 1,3 and 5 only

30) When a person finds that certain functions which he would like to perform are being done by some other person having a different role. It is called: A) role expectation conflict B) role overload C) role erosion D) role isolation

31) Type of compensation in which of the following is not matched properly: A) top or middle management – salary B) supervisors – salary C) clerical or administrative staff - salary D) unskilled, semi-skilled, skilled or highly skilled staff – wages

32) The compensation should be adequate which takes into account the following (1) minimum wages (2) living wages (3) fair wages (4) need-based minimum wages. A) 1 to 4 all B) 1 to 3 only C) 2, 3 and 4 only D) 2 and 4 only

33) What is meant by the term job evaluation?

A) it is a method for fix the compensation B) it is method of appraising the value or worth of one job incomparisonto other jobs in the organization. C) it is method of appraising the value or worth of one job in L-,comparison to other jobs in other organisations D) it is a method for fix the compensational aid for appraising the value or worth of one job in comparison to other jobs in the organisations.

34) Find out the incorrect statement: A) wages, salary and remuneration mean the same thing – false B) where the reward is linked to the performance, it helps in improvement of motivation level of employees – true C) uniform wage structure helps in improving the performance – false D) the remuneration to managerial position is referred to as salary - true

35) There are 2 methods for performance appraisal. Which of the following is correct, in this connection: A) the traditional methods emphasize on rating the individual personality traits B) the traditional methods lay importance on job achievement C) the modem methods lay emphasize on rating the individual personality traits D) none of the above

36 I)n the assessment center workshops method, in a job related simulated situation, the behavior of the employees is assessed through their. performance of different exercises such as A) group discussions, psychometric tests B) business games, committee meetings C) in-basket exercises

D) all the above

37) In the 360 degree appraisal method, the appraisal of an employee is done by:

A) seniors B) colleagues C) subordinates D) all the above

38) What is the objective of review by the superior of' the reporting authority in performance appraisal:

A) to eliminate the subjectivity B) to ensure the objectivity C) to minimise / reduce the bias or subjectivity D) to eliminate the bias

39) Which of the following statement is correct:

A) performance appraisal and potential appraisal are the same system B) performance appraisal is to know the future performance C) potential appraisal is to understand the potential of the employee to contribute to growth of organization D) none of the above

40)Counseling has 3 stages -1) recognizing the problem or issue , 2) Finding various alternatives to solve the problem, 3) Helping the employee to realize the problem & 4) Managing the Problem
A)1, 2 and 3 B)2, 3 and 4 C)1, 3 and 4 D) 1, 2 and 4
41)Information technology is the merger of (1) computers (2) human resources (3) communication.
A) 1 to 3 all B)1 and 2 only C) 1 and 3 only D) 2 and 3 only
42) For credit risk, the banks are presently following which of the following approach:
A)standardized approach B) basic indicator approach C) foundation internal rating based approach
D) advance internal rating based approach
43)Which of the following is an external factor leading to credit risk
A) bank branch failing to take adequate precaution in loan recovery B) bank policyregarding exposure, not having clarity C) change in RBI policy on rate of interest D)all the above
44) The due date for repayment of a term loan installment expires on feb 10, 2009 but borrower fails to make payment. The account becomes sub standard wef
A) May 13, 2009 B) May 12, 2009 C)May 11, 2009 D) May 10, 2009
45)Which of the following is correct in connection with classification of an account:
A) if account is out of order for more than 12 months, it becomes doubtful advance B) if account was sub standard for more than 3 months, it becomes doubtful advance C)if account was sub standard for more than 12 months, it becomes doubtful advance D) if account was sub standard for more than 36 months, it becomes loss account
46) A loan. account shows a balance of Rs.10 lac but the overdue recoverable amount is Rs.3.20 lac only beginning Oct 12, 2007. The borrower deposited Rs.3.40 lac on Feb 12, 2009. : A) account will be classified standard wef Feb 12, 2010 B) account will be classified standard wef Feb 12, 2009 C) account will be classified standard wef Feb 28, 2009 D) account will be classified standard wef Mar 31, 2009
47)Which of the following is not correct regarding CDR Standing forum: A) it is CDR policy making body B) Chairmen of all participating institutions / banks are its members C) RBI representative heads the CDR Forum D) it meets once in a 6 months period to review progress.
48)Which of the following cases are eligible under CDR mechanism: A) cases pending with Board for Industrial and Financial Reconstruction (BIFR) B) suit filed cases C) cases involving willful defaulters unless these are reviewed , D) cases involving fraud / misfeasance
49)Which of the following is correct regarding restructuring of SME accounts: A) package to be approved by the bank within 60 days B) accounts with potential viability within 10 years and repayment of restructured debt within 7 years are eligible C) additional amount of loan will be standard account for one year D) all the above
50) Sale of security under SARFAESI Act is possible when the possession of security is taken. Before Taking possession, a notice ofis to be given:
A)one week B)30 days C) 60 days D) at discretion of bank

Answers Test No.5

01	a	02	c	03	d	04	d	05	b
06	d	07	d	08	b	09	d	10	c
11	c	12	a	13	c	14	b	15	D
16	b	17	c	18	c	19	c	20	B
21	c	22	b	23	b	24	c	25	B
26	a	27	a	28	b	29	a	30	C
31	a	32	a	33	b	34	d	35	A
36	d	37	d	38	c	39	c	40	B
41	c	42	a	43	c	44	b	45	C
46	b	47	c	48	b	49	b	50	C

TEST YOURSELF : PRACTICE PAPER NO. : 1

1) Micro-economic theory studies how an economy determines.
a) The price of goods b)The price of services c)The price of economic resources d) All of the above.
2) A producer's positively sloped supply curve for a commodity represents.
a) In one sense a maximum and in another sense a minimum boundary of the.producer's intentions.A maximum boundary of

the producer's intentions. c)A minimum boundary of the producer's intentions. d) None of the above.

3) The theory of distribution refers to:

a) The distribution of income among various factors of the production. b)The distribution of income among different individuals in the economy.c) Both of the above d) None of these)

4) Interest is reward for parting with liquidity according to:a) B. Ohlin b)Von Haberler c) J.M. Keynesd) Alfred Marshall

5) Economics may be divided into macro-economics and micro-economics. Among the subject matter of micro economics may be found:The nature of value in exchange.b)The size of a country's national income c)The allocation of resources among competing uses d) The relative prices of specific services.

6) The statement that 'economics is positive and not normative' means:

a) That economics can be used to prove that capitalism is better than socialism.

b) That economics tells us what kind of economic behaviour or policy is wholesome and what evil

c) That economics tells policy makers which alternative to choose from among several efficient ones.

d) That economics can only indicate consequences of policies, choices, or conditions.

7) Which of the following statements is incorrect?

a) Micro-economics is primarily concerned with the problem of what, how and for whom to produce.

b) Micro-economics is primarily concerned with the behaviour of individual decision making units when at equilibrium.

c) MiCro-economics is primarily concerned with the time path and process by which one equilibrium position evolves into another

d) Micro-economics is primarily concerned with comparative static rather dynamics.

8) Economic laws may be described as:

a) Principles derived from an o;-.alysis of price am/ output determination.

b)Generations concerning the economic behaviour of individuals and institutions.

c) Forecasts in quantitative terms of the economic development of society.

d) Expression of the basic features of competition.

9) The main difference between positive economics and normative economics is that the former.

a) Discusses the ethical implications of its laws. b)Concerns itself only with hypotheses which can generally be tested.

c)Is based on the value judgements of economists. D) Considers carefully the political significance of its laws for a democratic society.

10) Adam Singh advocates:

a) Laissez-faire b)Division of Labour c)Both of the above d) None of the above

11) The term 'consumer goods' is used by economists to refer to:

a) Goods produced for consumers in a free market only. b)Goods other than free goods, whose use directly satisfies consumers wants. c)Goods produced by consumers in return for a wage. d) Goods which are used by consumers in order to earn their living

12) The basic characteristic of a C apitalistic economy is: a) Full employment b)The private ownership of the means of production.c)An absence of monopoly d) Large-scale production in primary industries.

13) In a free capitalist society the allocation of the factors of production among the various productive activities is determined by:a) The pattern of consumer's spending b)The traditional employment of facl= c)Decisions of the Government d) The wealth of the entrepreneurs.

14) Who believed that an automatic equilibrating mechanism of the perfectly competitive market, known as 'invisible hand' tended to maximize national wealth: a) Adam Smith b)Keynes c)J.B. Say d) None of the above

15) The fundamental economic problem being faced is one of: a)Consumer's choice b)Decision-making by the government c)'Multiplicity of wants and scarcity of resources. d) Shortage of labour.

16) Which one of the following is not directly the concern of the economist?

a) Aid to underdeveloped countries b)The effect of an increase in Bank rate c)The choice between alternative sites for a factory d) The use of taxation to discourage smoking of cigarettes.

17) The meaning of the word 'economic' is most closely connected with the word:

a) Free b)Scarce c)Unlimited d) Restricted

18) Which of the following is not an economic problem?

a) Deciding between extra paid work and extra leisure. b)Deciding between different ways of spending leisure lime .

c);:eciding on the level and form of personal saving d) Deciding between expenditure on one good and another.

19) Which one of the following statement is not true? A) Exchange is one method of helping to solve the basic economic problem. b)The basic ecolomic problem is one of choice. c)Choice is necessary because of Limited wants. d) The means to satisfy wants i.e., the factors of production, are limited.

20) Who gave scarcity definition of economics? a) Adam Smith b)Robbins c)Keynes d) J.B. Say

21) Who is known as the Father of Economics? a) Keynes b)Ricardo c)Adam Smith d) J.S. Mill

22) Many of the basic problems of economics emerge from:

a) Unlimited resources b)Incompetent govt. c)The use of limited resources to satisfy human wants d) Unlimited wants

23) The utility may be defined as: a)The power of a commodity to satisfy wants b)The desire for a commodity

c)The usefulness of a commodity d) The necessity of a commodity

24) The utility of a commodity is: **a)** Its expected social value b)Its relative scarcity c)he extent of its practical use d) The degree of its fashion

25) Marginal utility curve of a given consumer is also his:

a) Indifference curve b)Demand curve c)Supply curve d) Total utility curve

26) The total utility is maximum when: a) MU is zero b)AU is the highest c)MU is the highest d) MU is equal to AU

27) The law of diminishing marginal utility states that:

a) As more of a commodity is consumed total satisfaction diminishes.

b) The more you have of a particular commodity the less you want more of it.

c) As more units of a commodity are produced the price of the commodity will fall

d) The consumption of further units of a commodity will bring a steady thcrease in the amount of satisfaction obtained.

28) The law of diminishing returns or increasing cost will operate at an earlier level, in agriculture than in industry because:

a) More mechanization is applicable to agriculture b)Agriculture is an industry where land is used extensively

c)Less mechanization is applicable to agriculture. d) More labour is used in agriculture.

29) Opportunity costs are also known as: a) Spillover costs b)Alternative cost c)Social costs d) Money costs

30) An increase in the price'of a commodity, other things remaining same, results in:

a) Increase in pricina b)Increases in quantity supplied c)Increase in demand d) Taxes

31) Supply remaining constant, if demand increases, price will

a) Rise b)Remains constant c)Fluctuate d) Fall

32) Perfect competition is said to exist if: **a)**There are homogenous products b)Each firm in the industry accepts the market price because it has to accept it. c)Price is fixed not by a firm d) All of the above

33) Consumer's surplus is highest in case of: a) Luxuries b)Necessities c)Comforts d) Conventional necessities.

34) A "Giffen Goods" is one for which, in response to a small change in price. **A)** A zero income effect is just outweighed by a positive substitution effect. b)A negative income effect is just outweighed by a positive substitution effect. c)A zero income effect is matched by a zero substitution effect. d) A negative income effect outweighed any 'substitution effect.

35) Which is correct?

a) An "increase of demand" is not the same thing as an "extension of demand". b) An "increase of demand is the same thing as an "extension of demand". c) An increase of demand is just equal to the extension of demand. d) All the above statements are wrong e) An increase of demand invariably reduces the extension of demand.

36) Demand means:

a) The desire and willingness of an individual for all goods and services for his standard of living.

b) The desire, ability and willingness of an individual to purchase goods and services at a given time and price

c) Both A and B d) None of the above

37) The demand function for a commodity is defined as: **a)** Quantity demanded as a function of the goods, own price, the price of the substitute and the buyer's income **b)** Price of Substitutes as a functions of the goods own prices **c)** Quantity demanded as a function of tne price of other goods d) d) All the above

38) In the typical demand schedule, quantity demanded.

a) Varies directly with price. **b)** Varies proportionately with price **c)** Is independent of price **d)** Varies inversely with price

39) Law of demand states that when:

A) Income rises demand rises. b)Price rises demand rises. c)Price falls demand falls. d) Price falls demand rises

40) The law of demand indicates**: a)** The relationship between income and quantity demanded **b)** The relationship between price of a commodity and price of ifs cubstitutes **c)** The relationship between price of two commodity. **d)** The relationship between the price of commodity and the quantity demanded.

41) Which of the following conditions is required condition for the operation of law of demand? a) Price of subStitute change b) Income and Taste of consumer remains constant c) Production does not increase d) Taste of the consumer change

42) Demand curve shows:

a) Inverse relationship between quiantitydemailed and its cost of production.

b) Inverse relationship between the rate of change of demand and price.

c) Inverse relationship between the rate of change in demand and cost of production at a given times.

d) Direct relationship between the demand and the price of a commodity at a given time.

43) When we say that a demand curve for a commodity slopes downwards to the right we mean:

a) More of the commodity will be demanded as income increase

b) More of the commodity will be demanded as the price of the substitutes falls.

c) More of the commodity will be demanded as population rise.

d) More of the commodity will be demanded as its own price falls.

44) A fall in the price of a commodity leads to:

a) A shift in demand b)A fall in demand c)A fall in the consumers real income d)A rise in the consumers real income

45) An exceptional demand curve is one that slopes:

a) Upward to the lift b)Upward to the right c)DoWnward to the right d)Horizontal
46) Which one is not an exception to the Law of Demand?
a) Ignorance b)Inferior good c)Normal good d) Articles of Distinction
47) Demand for a commodity is elastic when has:
a) Only one use b)Many Use c)Uses, which cannot be postponed d) Uses very essential for the consumer
48) Which of the following pairs of commodities is an example of substitute:
a) Coffee and milk b)Mustard oil and coconut oil c)Diamond and cow d) Pen and ink
49) For most customers apples and oranges are substitute goods. Therefore, we would expect a rise in the price of apples to lead to: a) A rightward shift in the supply curve of oranges b)A leftward shift in the supply curve of oranges.
C)A fall in the price of oranges d) An upward change in the demand curve of oranges.
50) A change in climate,conditions resulting in hot weather, price remaining the same, would cause a consumer of cold drinks: a) To move to a lower demand curve b)To move lower down the demand curve c)To move to a higher demand curve d)To move up the same demand curve
51) When an individual's income falls (while everything else remains the same) his demand for an inferior goods:
a) Increase b)Remaining unchanged c)We cannot say without additional information d) Decrease
52) A fall in the price of a commodity whose demand curve is a rectangular hyperbola causes total expenditure on the commodity to:
a) Remain unchanged b)Increase c)Decrease d) Any of the above
53) The relationship between demand for a commodity and price, ceteris paribus, is:
%a) Negative b)Positive c)Non-negative d) Non-positive
54) Other things being equal a decrease in the quantity supplied to the market at given prices leads to:
a) A higher price and a contraction of demand b)A higher price and an expansion of demand. c)A higher price and an expansion of demand d) A lower price and a contraction of demand.
55) Law of demand explains:
a) Quantitative relationship between price and demand b)Qualitative relationship between price and demand c)Relationship between demand and supply d) Rate of change in price and demand
56) We can say with certainty that when the demand for TVs increases in the long run, prices:
a) Will go down b)Will go up c)Change proportionately d) Cannot be predicted with the knowledge of elasticity of demand
57) In the normal demand schedule, quantity demanded:
a) Varies directly with price b)Is independent of price c)Varies inversely with price d) Varies proportionately with price
58) An example of derived demand is demand for: a) Pen and ink b)Wool and mutton c)Petrol and Car d) None of the above
59) By increase in demand we mean: a) Movement upwards on a demand curve b)Movement downwards on demand curve c)Shifting upwards of a demand curve d)None of these
60) Law of demand operates because of a) Price changes b)The principle of different income c)Changes in advertisement expenses d) None of the above
61) Multiple uses of a commodity will make the demand go up when:
a) Price increases b)Price remains the same c)Price falls down d) None of the above
62) Status symbol goods are:
a) Veblen goods, b)Exception to law of demand, c)Goods of conspicuous consumption,d) ALL OF THE ABOVE
63) Price - demand relationship in the case of Giffen goods is: a) Inverse•b)Direct c)Absent d) None of the above
64) The downward sloping demand curve may be partly explained by the "income effect" which refers to:
a) People's tendency to save more as their real incomes fall in the short period.
b) An increase or decrease in the amount of a good purchased because of a price-induced change in the purchasing power of a fixed income.
c) Changes in the relative importance of good purchased because of changes in the con imunity's tastes resulting from adverting.
d) Changes in the distribution of income in a community.
65) The demand curve for a commodity is generally drawn on the assumption that:
a) The commodity has no substitutes b)Tastes, income and aii other prices remain constant. c)The average household consist of two persons d) Purchases of the commodity are made by a free market.
66) A fall in the price of a commodity leads to:
a) A shift in demand b)A fall in demand c)A rise in consumer's real income d) A fall in the consumer's real income.
67) In the case of Giffin good like Bajra a fall in its price tends to: a) Make the demand remain constant b)Reduce the demand c)Increase the demand d) Li) Change demand in an abnormal way.
68) Which of the following pairs of commodities is an example of substitutes:
a) Coffee and milk b)Diamond and cow c)Pen and ink d) Mustard oil and coconut oil.
69) For most consumers apples and oranges are substitute goods. Therefore, we would expect a rise in the price of apples to lead to: a) A rightward shift in the demand curve of oranges b) A leftward shift in the supply curve of apples

c) A downward change in the demand curve of oranges **d)** A fall in the price of oranges
70) A change in climatic conditions resulting in hot weather, price remaining the same, would cause a consumer of cold drink: **a)** To move to a higher demand curve **b)** To move up the same demand curve
c) 1 o move lower down the curve **d)** To move to a lower demand curve.
71) If two goods are complementary, this means that a rise in the price of one commodity will induce:
a) An upward shift in demand for the other commodity **b)** A rise in the price of the other commodity
c) A downward shift in demand for other commodity **d)** No shift in demand for the other commodity.
72) If more is demanded at the same price or same quantity at a higher price, this fact of demand is known as:
a) Extension of demand **b)**Increase of demand **c)**Contraction of demand **d)** Decrease of demand.
73) Other things being equal a decrease in demand can be caused by:
a) A rise in the price of the commodity **b)** A rise in the income of the consumer **c)** A fall in the price of the commodity
d) A fall in the income of the consumer
74) An increase in demand can result from:
a) A decline in market price **b)** An increase in income **c)** A reduction in the price of substitutes **d)** An increase in the price of complementary goods **e)** All the above
75) Which of the following circumstances would be likoly to bring about a change in the demand schedule for a product?
a) A fall in the price of the product **b)** An increase in the number of potential consumers
c) A new method of producing the product **d)** An increase in the quantity produced. **E)** Both a &b
76) If the price of good A affects the demand for good B, then:
a) A is a substitute for B **b)** B is complement of A **c)** Changes in the price of A will cause movement along the demand schedule for A **d)** Changes in the price of B will not change the demand for A. **e)** Changes in the price of A will shift or change the demand for B.
77) Cross demand is the change in the quantity demanded of a given commodity in response to the:
a) Change in the utility of another commodity **b)** Change in the price of another commodity
c) Change in the nature of another commodity **d)** Change in the size of another commodity.
78) The law of demand states that:
a) Demand increases with increase in income **b)** When income and prices rise. the demand also rises
c) When income and prices rise. the demand also rises **d)** When price increases, demand increases
79) A consumer's equilibrium choice or position is one at which:
a) His savings are maximized **b)** His assets are maximized
c) His satisfaction is maximum **d)** Price of goods is maximised
80) For most consumers, milk and tea are substitute goods. Ther-fore, we should expect a rise in price of milk to lead to:
a) A rightward shift in the supply curve of tea. **b)** A leftward shift in the supply curve of tea.
c) A fall in the price of tea. d) An upward shift in the demand curve for tea.
81) Other things being equal, a fall I contraction in demand can be caused by a:
a) Rise in prices of the substitute b) Rise in prices of the substitute c) Rise in prices of the substitute d) Rise in the income of the consumer **e)** Rise in the price of the commodity
82) The demand for a good is elastic if:
a) The demand for that good increases when price falls b) A decrease in price results in a decrease in total expenditure
c) The quantity demanded increases less than proportionately with the decrease in price level
83) A rightwards shifts in supply schedule indicates:
a) A decrease in Supply **b)**A decrease in quantity supply **c)** An increase in quantity supply **d)** An increase in supply.
84) A rightwards shift in supply curve indicates:
a) A decrease in supply **b)**An increase in quantity supplied **c)** An increase in supply **d)** None of the above
85) A supply curve will generally take an upwardsslopin9 form left to right because:
a) Market price is normally above total costs of production. **b)**Consumers' income tend to increase in the long period.
c) Producers' costs tend 'to increase as their output expands **d)** Supply of most goods is essentially a short-term phenomenon.
86) Other things being equal an increase in supply can cause by:
a) A rise in the price of the commodity **b)**An improvement in the techniques of production
c) A rise in the income of the consumer **d)** An increase in the income of the seller.
87) The shift of the supply curve for a commodity to the left may indicate, other things being equal, that:
a) Shares in the producing firms are in great demand on the Stock Exchange. b) Producers of the commodity wish to make and sell less at same price. c) Prices raw materials used in the production of the commodity have fallen. d) Wages paid to the producers' employees have fallen.
88) Ceteris paribus, a decrease in quantity supplied of a commodity can be caused by:
a) A fall in its price **b)**Fall in income **c)**Rise in price **d)** Fall in raw material
89) The supply schedule for a commodity is usually assumed to be directly open to influence by all the following except:
a) The quantity demanded **b)**The prices of the factors of production **c)**The costs of production **d)** The prices of other goods

90) Which of the following could explain why the supply curve for a commodity slopes downwards?
a) Producers do not like increasing production. **b)**Producers have to lower price to induce consumers to buy more **c)**Costs fall as production increases **d)** Diminishing marginal utility is in operation

91) "Free Trade Area" denotes:
a) Pitlicy of Laissez faire
b) A group of countries which have decided to impose no duties of any kind on imports from other members of the group
c) Free Exports & Imports **d)** All the above

92) Temporary control of inflation can be effected by:
a) Lowering Bank Rate **b)**Purchasing of securities by RBI **c)** Restraint on the growth of money supply **d)** None of these

93) The term "hyper-inflation" is used to denote:
a) Creeping inflation **b)**Step by step inflation **c)** A "Runaway" or "galloping" inflationary situation where the monetary unit becomes almost worthless **d)** None of these

. 94) In calculating a country's GNP at market prices one of the following is not included:
a) Depreciation **b)**Net factor income from abroad **c)**Net indirect taxes **d)** Transfer Payment

95) Indian Economy can be best described as:
a) Developed economy **b)**Undeveloped economy **c)**Developing economy **d)** Underdeveloped

96) The term "balance of trade" means:
a) Difference between exports & imports **b)**Net Exports including merchandise **c)**The difference between the cost of the imports and exports of a country. **d)** a and c

97) The open market operations refer to the sale and purchase by the RBI of:
a) Foreign exchange **b)**Gold **c)**Government securities **d)** All c' the above

98) At full employment level, which of the following would be most likely to lead to inflation?
a) A fall in taxation with no changes in gevemment expenditure **b)**An increase in productivity without any increase in wages **c)**A fall in investment with no change in prosperity to consumer **d)** A rise in the prosperity to save with no change in investment

99) Deflation is:
a) Deficit budget **b)**Reduction in taxation **c)**Contraction in volume of money or credit that results in a decline of price level **d)** Increase in public expenditure

100) Bank rate means:
a) Interest rate charged by moneylenders, **b)**Interest rate charged by the scheduled banks **c)**Rate of profit of the banking institution **d)** The official rate of interest charged by the central bank of the country

ANSWER ; PRACTICE PAPER NO. : 1

1	D	2	A	3	B	4	C	5	C	6	D	7	A	8	B	9	B	10	C
11	B	12	B	13	A	14	C	15	C	16	C	17	C	18	B	19	C	20	B
21	C	22	C	23	A	24	B	25	B	26	A	27	B	28	B	29	B	30	B
31	A	32	D	33	B	34	B	35	A	36	B	37	A	38	D	39	D	40	D
41	B	42	B	43	D	44	D	45	B	46	C	47	B	48	B	49	D	50	C
51	C	52	A	53	A	54	B	55	C	56	D	57	C	58	D	59	C	60	A
61	C	62	D	63	B	64	B	65	B	66	C	67	B	68	D	69	A	70	A
71	A	72	B	73	D	74	B	75	E	76	E	77	B	78	C	79	C	80	D
81	D	82	C	83	D	84	C	85	C	86	D	87	B	88	A	89	A	90	C
91	B	92	C	93	C	94	D	95	C	96	D	97	D	98	A	99	C	100	D

TEST YOURSELF : PRACTICE PAPER NO. : 2

1) In the Keynes model above, which is independent:
a) Investment **b)**Consumption **c)**National income **d)** Consumption and investment

2) How many motives for demanding money has been given by Keynes:
a) 1 **b)**2 **c)**3 **d)** 4

3) Recession is associated with fall in:

a) Demand b)Supply c)Disinvestment d) Investment

4) Devaluation means:

a) Fall in Marginal utility of Money b)Fall in printing of currency c)Risk in black money d) Fall in the value of money in terms of foreign currency

5) Acute inflationary situation:

a) Makes savings in the form of bank deposits less attractive b)Makes savings more attractive

c) Arises due to liquidity trap d) All the above

6) Inflation means:

a) Increase in price b)Decrease in value of money c)Boom d) All of the above

7) The problem of unemployment in rural areas is mainly due to:

a) Seasonal and under employment b)Frictional unemployment c)Structural unemployment

d) Technical Lriernpleyrnent

8) NNP for a given year can be defined as:

a) Market value of final goods only b)The market value of all final goods and services c)The market value of all final services only d) None of the above

9) LiqUidity preference is the term, which is used to refer to:

a) The Reserve Bank of India's shareholdings in other financial institutions

b) The extent to which investors prefer to keep their assets in money

c) The community's preference for a gold-backed currency

d) An inducement to save.

10) Which of the following are among the major determinants of the interest rate in the Keynesian theory?

a) People's desire to hold money and to keep their wealth in liquid form b)The available stock of money

c)The intensity of speculation on the stock exchange d) The value of gold and silver on the world's markets

11) The famous book written by J.M. Keynes is entitled:

a) Principles of Economics b)Law of Markets c)The General Theory of Employment, Interest and Money d)None of the above.

12) To's layman, investment means putting his money in a financial asset like bonds, fixed deposit etc. What does it mean to an economist:

a) Purchase of machines b)Stock of durable goods c)Purchase of real capital assets d) All of the above

13) The liquidity preference arises due to:

a) Transaction Motive b)Precautionary Motive c)Speculative Motive d) All of these

14) Liquidity trap is likely to result when:

a) Rate of Interest at its lowest b)Rate of Interest at its highest c)No change in supply of money d) When an increase in the supply of money fails to reduce the rate of interest

15) Which theory is called the Neo-Classical theory of rate of interest?

a) Risk Theory b)Liquidity Preference Theory c)a and b d) Loanable Funds Theory.

16) The agency estimating the National Income of India is:

a) Reserve Bank of India b)Planning Commission c)Ministry of Finance d) Central Statistical Organisation

17) The goals of monetary policy do not include

a) Maximum output b)Full ernploymeot c)Price stability ,d) Maximum tax revenue

18) Gross National Product (GNP) is:

a) The total output of goods and services produced by the country's economy

b) The total domestic and foreign output claimed by residents of the country

c) The sum of gross domestic product and investment

d) National income minus national expenditure

19) If an economy is in equilibrium at the point where plans to save and to invest are equal, then government expenditure must be:

a) Curtailed b)Equal to government income c)Increased d) None of the above

20) Which of the following is correct regarding the gross domestic savings in India?

a) Contribution of corporate sector is largest b)Contribution of government sector is the largest

c)Contribution of household sector is the largest d) None of these

21) NNP (Net National Product) or National Income is the money value of

a) Final goods and services produced annually in the economy b)Annual service generation in the .economy

c)Tangible goods produced annually in the economy d) Tangible goods available in the economy

22) Which of the following is included in the calculation of gross domestic product?

a) Personal consumption expenditure b)Gross domestic investment c)Purchase by the government d) All of the above

23) Gross National Product is greater than gross domestic product when:

a) NFI (from abroad) > 0 b)NFI < 0 c)NFI = 0 d) NFI = -1

24) Which of the following is deducted from gross national product in order to estimate net national product?

a) Depreciation **b)**compensation of employees **c)**expenditure on buildings **d)** expenditure on raw material

25) Changes in the standard of living in a country are best reflected in changes in the:

a) Social Welfare **b)**Economic Welfare **c)**Per capita income at current prices **d)** Per capital income at constant prices

26) Whicl: is the primary indicator to recognise a country's rate of economic growth?

a) Increase inter per capita income **b)**Setting of more industries **c)**Rate of growth in national income d) More exports

27) National Income is based on:

a) Total Production x prices **b)**Rent + wages + Interest ,+ Profit **c)**Domestic Income + NFI **d)** The sum of all factor incomes **e)** All the above

28) Net National Production excludes:

a) Gross Investment **b)**Net investment **c)**Foreign Investment **d)** Replacement investment

29) Here are four statements about various national income / expenditure I product relationships. Which one of the following is true:

a) GNP less NIT = NNP **b)**GNP less NFI = NNP **c)**GNP plus depreciation = NNP **d)** GNP less depreciation allowances = NNP

30) The term GDP incorporates the economic activity:

a) Taking place within the geographical boundary of the country, **b)**Within the land territorial **c)**Within water territorial, **d)** Within air space

31) The term "Hindu rate of growth" refers to the 3.5% per annum growth rate achieved by the Indian economy over the first six Five-Year Plans. The term was coined by

a) Chakravaty **b)**J.N. Bhagwati **c)**Raj Krishna **d)** K.N. Raj

32) Essential services owned and controlled by government is called:

a) Public monopoly **b)**Public utility **c)**Public Sector**d)** All of the above

33) Which of the following is not a fiscal monopoly?

a) Printing of currency **b)**Minting of coins **c)** Electricity supply **d)** None of the above

34) In a planned economy the economic problem of what shall be produced is determined primarily by:

a) Computers deciding what consumers want. **b)**Direction by the oovernment.**c)**The pattern of consumer's spending **d)** The independent decisions of entrepreneurs.

35) Development means economic growth plus: **a)** Price stability **b)**Social change **c)**Inflation **d)** Deflation

36) Which Plan recommended Zero-Based Budgeting (ZB**B)**as a step to control public expenditure?

a) Fifth Plan **b)**Sixth Plan **c)**Seventh Plan **d)** Eighth plan

37) All revenues received, loans raised and money received in repayment of loans by the Union Government go into.

a) Public Account of India **b)**Contingency Fund in India **c)**Consolidated fund in India **d)** none of the above

38) Which one of the following is not directly the concern of the economist?

.**a)** Choices relating to location of a steel plant **b)**Bargaining between the workers' unions and the employers **c)**Effects of a change in money supply. **d)** Imposition of tax to discourage cigarette smoking

39) Customs duties, export duties, corporation taxes, taxes on capital value of assets (excluding agricultural land of individuals and companies) are:

a) Taxes and duties levied by the Centre but wholly appropriated by the States

b) Taxes and duties levied by the Centre but collected by the States

c) Taxes and duties that accrue wholly to the Union Government

d) Taxes levied and collected by the Union but which are shared with the States.

40) "Funded debt" means:

a) All Government securities which are marketable on the stock exchange market **b)**All private securities , **c)**Shares of Companies **d)** KisanVikasPatras

41) "Annual Financial Statement" is another name of:

a) Balance of payment **b)**Fiscal Budget ,**c)**Budget **d)** Debt & Credit

42) "Multi-Currency Basket" means:

a) Relationship with world bank **b)**Currency + coins **c)**Number of major international currencies to which the external value of the Indian rupee is linked **d)** None of the above

43) Which of the following is not a seiective credit control measure?

a) Rationalizing of Credit **b)**Open market observations **c)**Changes in the statutory liquidity ratio **d)** a and c

44) Public finance is said to be:

a) Science of taxes and pending **b)**Science of demand and supply of money **c)**Science of money and cost **d)** Science of income and expenditure

45) One of the distinctions between public finance and private finance is that:

a) The State adjusts "income to expenditure' while an individual adjusts "expenditure to income"

b) The State maximizes the general welfare of the public while an individual maximizes his own satisfaction

c) The State has no coercive powers while the individual has

d) The State cannot borrow money while the individual can get loans

46) A tax takes away a higher proportion of one's income rise is termed is:
a) Proportional Tax b)Indirect Tax c)Regressive Tax d) Progressive Tax
47) Corporate tax is imposed by: -
a) Local Government b)Central Government c)State Government d) Both Central and State Government
48) Which of the following are direct taxes?
a) Gift tax b)Income tax c)Corporation tax d) All of the above
49) From the following, which is not a direct tax?
a) Tax on wealth b)Tax on entertainment c)Tax income d) Tax on expenditure
50) An Direct tax is one where:
a) Tax is levied always on property b)Points of impact and incidence are different
c)Tax is levied on wealth d) Points of impact and incidence are the same
51) The name of Indirect tax is:
a) Income tax b)Sale tax c)Corporate tax d) Wealth tax
52) A regressive tax will tend to redistribute income more:
a) Equally b)Equitably c)Unequally d) Inequitably
53) Which of the following does not grant any tax rebate?
a) Indira VikasPatra b)Public Provident Fund c)National Saving Scheme d) National SavingCertificate
54) The Indian Income tax is:
a) Direct and progressive b) id re arid oev$_u$;essive c)Indirect and proportional d) Direct and proportional
55) Temporary tax levied to obtain additional revenue is called:
a) Fee b)Surcharge c)Cess d) Rate
56) Which of the following taxes is/are levied by the Central Govt. and collected appropriated by the States?
a) Estate Duty b)Stamp Duties c)Passenger and goods tax d) Taxes on Newspaper
57) Taxes raised are credited into:
a) Consolidated Fund b)Public Accounts c)Contingency Accounts , d) Private Accounts
58) Generally tax on production are:
a) Indirect taxes b)Both A and B c)Direct taxes d) None of the above
59) Tax on incomes is:
a) Indirect b)Both A and B c)Direct d) None of the above
60) Which of the following taxes is levied on services?
a) Personal tax b)Value added tax c)Capital gains tax d) Corporate tax
61) Income tax is raised by:
a) Local Government b)Central Government c)Municipality d) State Government
62) Sales tax is levied by:
a) Local government b)State government c)Central government d) None of the above
63) Union Excise Duties are a part of Central Government's:
a) Tax revenue b)Capital receipts c)Non-tax revenue d) None of the above
64) All taxes come under:
a) Capital receipts b)Revenue receipts c)Public debt d) Both A and C
65) In India, the States gets maximum income from:
a) Sales tax b)State Excise duties c)Land Revenue d) Agricultural Income tax
66) Progressive tax in India is:
a) Income tax b)Wealth tax c)Corporate tax d) Sales tax
67) Which of the following is a direct tax?
a) Sales tax b)Entertainment tax c)Excise duty d) Estate duty
68) Which of the most important source of revenue to the State Government of India ?
a) Land Revenue b)Agriculture Income-tax c)State excise duties d) Sales tax
69) A budget is the summary of:
a) Proper allocation of resources b)Income reallocation c)Resource reallocation d) Revenue and expenditure
70) The budget deficit refers to the difference between all-revenue and expenditure of:
a) Revenue account only b)Increased government expenditure c)Capital account only d) Both revenue and capital accounts
71) Borrowing from capital market is a part of:
a) Revenue budget b)Capital budget c)Both a and b d) None of these
72) Revenue deficit in India is:
a) Negative b)Positive c)Zero d) None of 'he above
73) Capital deficit in India is:
a) Positive b)Zer'.3 c)Negative d) None of the above
74) Funds, which do not belong to the government, are?

a) Consolidated fund b)Contingency fund c)Public accounts d) None of the above
75) Which budget in India is passed separately?
a) Airlines b)Railways c)Defence d) Atomic energy
76) Which one of the following cannot be influenced by budgetary policy?
a) Power of private monopolies b)Balance of trade c)General level of prices d) Regional distribution of employment
77) Which budget is measured in financial terms only?
a) Dominance budget b)Programme performance budget c)Zero-base budget d) Central budget
78) Deficit Financing means:
a) Government spends in excess of revenue and capital receipt to that budget deficit in incurred which is financed by borrowing from the RBI. b)niffpropra of total expenditure inc$_o$me anti.. income by revenue from all sources. c)Difference in borrowing an internal and external resources d) Capital expenditure on items of public construction, public enterprises and public borrowings.
79) The need for deficit financing in India arises due:
a) Failure of the government to mobilize the desired volume of surplus for the public sector plans.
b) The rapidly growing expenditure incurred by the government c) Neither A nor B. ' d) Both A and B
80) Deficit financing leads to:
a) Inflation b)Capital formation ,c)Neither A nor B d) Both A and B
81) Deficit financing means:
a) Difference in borrowing and internal and external resources
b) Capital expenditure on items of public construction, public enterprises and public borrowings
c) Government spends in excess of revenue and capital receipts so that budget deficit is incurred which is financed by borrowing from the RBI.
d) Difference of total expenditure and income by revenue from all sources
82) The effect of deficit financing is:
a) Never inflationary b)Always inflationary c)Sometimes inflationary and sometimes not so depending cn conditions of the economy and the dose of deficit financing. d) None of these
83) The direct effect of deficit financing is:
a) Deficit financing leads to extra money supply which in turn pushes up prices
b) Demand and supply both increase c)The price situation comes under complete control d) Deficit financing leads to extra money supply, which in turn makes market more & more competitive.
84) Fiscal policy is related to:
a) Exports and Imports b)Public revenue and expenditure c)Issues and circulation of currencies d) Monetary Control measures
85) A restrictive monetary-fiscal policy is a good way to deal with:
a) Demand — shift inflation b)Any short of inflation that occurs when the economy falls below full employment
c)Demand — pull inflation, d) Cost — push inflation
86) Grants—in-aid given by the Centre to the states is meant:
a) To cover the gaps on revenue accounts. b)For flood control
c)Po(boosting agriculture in the State. d) For financing State plan projects
87) The finance commission is appointed every:
a) 7 years b)6 years,'C)5 years d) 3 years
88) The Narsimham Committee submitted its report to the government on:
a) Depoliticising appointments in public sector undertakes Import and eYportrestrnrtliring '"d) Banking structure
89) "Interest is the reward for pure waiting." Which theory of interest explains it?
a)Time Preference Theory b)Classical Theory c)Liquidity Preference Theory d) Loanable Funds Theory
90) What is not true for the Classical theory of interest?
a) Demand and Supply Theory b)Saving-Investment Theory c)Non-monetary Theory d) Monetary Theory of Interest
91) The Loanable Funds Theory of interest is also known as:
a) The neo-classical theory of interest,b)The classical theory of interest c)The real theory of interest,d)The modern theory of interest
92) Rate of interest is a function of I, S, M, r = f (I, S, M, L) is explained by which of the following theories? A)Liquidity Preference Theory, b)Saving-Investment Theory c)Loanable Funds Theory d) Modern Theory
93) For which of the following motives for liquidity preference, the demand for liquidity is determined by the rate of interest? a) Transaction motive b)Precautionary motive c)Speculative motive d) All the three motives.
94) Which of the following is known as monetary theory of interest?
a) Loanable Funds Theory b)Modern Theory, c)Liquidity Pi eference Theory,d) Saving-Investment Theory
95) What is not true of the modern theory of interest?
a) Neo-Keynesian Theory b)Hicks and Hansen's synthesis c)Monetary Theory d) IS-LM Curves Analysis
96) Which of the following is not a characteristic of business cycles?

a) Recurrent in nature b)Periodicity ,c)Regular d) Cumulative

97) Who gave innovation theory of business cycles ?

a) Pigou b)I. A. Hobson, c)Schumpeter d) J. Tinbergen

98) Which of the following assumptions is not correct in relation to Hicks' theory of business cycle ?

a) The equilibrium of the economy is influenced by changes in consumption and investment

b) Fall employment is the ceiling of expansion c) Autonomous investment increases at some constant rate even during depression d) Accelerator remains operative in all phases of business cycle, but the multiplier stops operating during depression

99) Economic growth refers to :

a) An increase in per capita income at current prices, b)A sustained increase in per capita output

c) An increase in income and output in real terms and not in money d) An increase in economic welfare

100) National income differs from NNP at market prices by the amount of :

a) Current transfers from the rest of the world, b)Net indirect taxes, c)National debt interest, d) It does not differ

ANSWER ; PRACTICE PAPER NO. : 2

1	A	2	C	3	A	4	D	5	A	6	B	7	A	8	B	9	B	10	C
11	C	12	C	13	D	14	A	15	D	16	D	17	D	18	B	19	B	20	C
21	A	22	D	23	A	24	A	25	D	26	C	27	E	28	D	29	D	30	A
31	C	32	D	33	C	34	B	35	B	36	C	37	C	38	A	39	C	40	A
41	C	42	C	43	D	44	D	45	A	46	D	47	B	48	D	49	B	50	B
51	B	52	C	53	A	54	A	55	B	56	A	57	A	58	C	59	C	60	B
61	B	62	B	63	A	64	B	65	A	66	A	67	D	68	D	69	D	70	D
71	B	72	A	73	A	74	C	75	B	76	A	77	B	78	A	79	D	80	D
81	C	82	C	83	A	84	B	85	B	86	A	87	C	88	D	89	B	90	D
91	A	92	C	93	C	94	C	95	C	96	C	97	C	98	D	99	B	100	B